Supreme Court, U. S.
FILED
DEC 1 1976
MICHAEL RODAK, JR., CLERK

In the Supreme Court of the United States

OCTOBER TERM, 1976

No. 76-7514

KOEHLER MANAGEMENT CORP., GERALD KOEHLER, ROGER BENHAM, WILLIAM J. EISENHAUER, PAUL M. GILLMOR, MARTIN A. JANIS, ROBERT B. JOHNSTON, RAY W. MOLDER, ALFRED E. RHODEN, M.D., GILBERT H. SIEGEL, RAY L. VISCHER, ESTATE OF JOSEPH A. SCHUSTER, DECEASED,

Petitioners,

vs.

CHARLES NICKELS and MARGARET NICKELS on Behalf of Themselves and All Other Shareholders of Koehler Management Corporation,

Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

STANLEY GOODMAN
RONALD K. RYCHENER
GOODMAN & GOODMAN CO., L.P.A.
1016 Fourth & Walnut Building
36 East Fourth Street
Cincinnati, Ohio 45202
(513) 621-1503
Attorneys for Petitioners

E. L. MENDENHALL, INC., 926 Cherry Street, Kansas City, Mo. 64106, (816) 421-3030

TABLE OF CONTENTS

CITATIONS II

OPINIONS BELOW 2

JURISDICTION 2

QUESTION PRESENTED FOR REVIEW 2

STATUTES AND RULES INVOLVED 2

STATEMENT OF THE CASE 3

1. Factual Background 3
2. Proceedings Below 4

REASONS FOR GRANTING THIS WRIT 5

I. The Sixth Circuit's Application of the Four Year State Statute of Limitations Governing Common Law Fraud Actions Instead of the Two Year State Blue Sky Statute of Limitations Has Created a Direct Conflict With Recent Decisions of the Fourth, Fifth, Seventh, and Eighth Circuits Regarding the Applicable State Statute of Limitations for Implied Rights Under the Federal Securities Laws 5

II. Under the Resemblance Test, Ohio Revised Code Section 1707.43 Best Effectuates Federal Policy 12

III. The Federal Policy Underlying the Implied Remedies Found in Section 10(b) and Section 17(a) Would Be Better Effectuated by Application of the Statutes of Limitation Found in Other Federal Securities Provisions, Rather Than Those That Apply to State Common Law Fraud 17

A. The Application of State Statutes of Limitation Results in Unfair Distinctions Between Plaintiffs in Different States 17

B. Federal Policy Can Best Be Determined by Examining the Statutes of Limitation Adopted

by Congress for Express Rights of Action Under the Securities Laws 18

CONCLUSION 20

APPENDIX—

Opinion, United States Court of Appeals, Sixth Circuit A1

Opinion and Order, United States District Court, Northern District of Ohio, Western Division A17

Federal Securities Laws A27

Ohio Revised Code A32

Citations

Cases

Aboussie v. *Aboussie*, 441 F.2d 150 (5th Cir., 1971) 17

Affiliated Ute Citizens v. *United States*, 406 U.S. 128 (1972) 15

Bailes v. *Colonial Press, Inc.*, 444 F.2d 1241 (5th Cir., 1971) 17

Batchelor v. *Legg & Co.*, 52 F.R.D. 553 (D. Md., 1971) 11

Beamer v. *Feick*, 113 O.App. 264, 177 N.E.2d 691 (Erie Co., 1960) 15

Berry Petroleum Co. v. *Adams & Peck*, 518 F.2d 402 (2d Cir., 1975) 11

Butterman v. *Steiner*, 343 F.2d 519 (7th Cir., 1965) 17

Campbell v. *City of Haverhill*, 155 U.S. 610, 39 L.Ed. 280 (1895) 5

Charney v. *Thomas*, 372 F.2d 97, 100 (6th Cir., 1967) 5, 6, 7, 9

Connelly v. *Balkwill*, 174 F. Supp. 49 (N.D. Ohio, 1959), *aff'd per curiam*, 279 F.2d 685 (6th Cir., 1960) 6, 7, 12

Corey v. *Bache & Co.*, 355 F. Supp. 1123 (S.D. W.Va., 1973) 11

Crane v. *Courtright*, 2 O.App.2d 125, 206 N.E.2d 913 (Franklin Co., 1964) 15

Denny v. *Performance Systems, Inc.*, [1971-1972 Transfer Binder] CCH Fed. Sec. L. Rep. para. 93,387 (M.D. Tenn., 1971) 17

Dudley v. *Southeastern Factor and Finance Corp.*, 57 F.R.D. 177 (N.D. Ga., 1972) 17

Ernst & Ernst v. *Hochfelder*, ... U.S. ....., 47 L.Ed. 2d 668, 96 S.Ct. ..... (March 30, 1976) 15

Fischman v. *Raytheon Manufacturing Company*, 188 F.2d 783 (2d Cir., 1951) 17

Hitchcock v. *deBruyne*, 377 F. Supp. 1403 (D. Conn., 1974) 11

Hudak v. *Economic Research Analysts, Inc.*, 499 F.2d 996 (5th Cir., 1974), *cert. denied*, 419 U.S. 1122 (1975) 7, 9, 14

IDS Progressive Fund, Inc. v. *First of Michigan Corporation*, 533 F.2d 340 (6th Cir., 1976) 12

Josef's of Palm Beach, Inc. v. *Southern Inv. Co.*, 349 F. Supp. 1057, 1060 (S.D. Fla., 1972) 11

Kramer v. *Loewi & Co.*, 357 F. Supp. 83, 87 (E.D. Wis., 1973) 11

McIntyre v. *The First National Bank of Cincinnati*, 541 F.2d 611 (6th Cir., 1976) 2, 5

Morgan v. *Koch*, 419 F.2d 993 (7th Cir., 1969) 17

Newman, et al. v. *Prior*, 518 F.2d 97 (4th Cir., 1975) 9, 10

Charles Nickels, et al. v. *Koehler Management Corporation, et al.*, 541 F.2d 611 (6th Cir., 1976) 2

Parrent v. *Midwest Rug Mills, Inc.*, 455 F.2d 123 (7th Cir., 1972) 7, 8, 9, 17

Saylor v. *Lindsley*, 391 F.2d 965 (2d Cir., 1968) 17

United Auto Workers v. *Hoosier Cardinal Corp.*, 383 U.S. 696, 16 L.Ed.2d 192 (1966) 5
United California Bank v. *Salik*, 481 F.2d 1012 (9th Cir., 1973), *cert. denied*, 414 U.S. 1004 (1973) 11
Vanderboom v. *Sexton*, 442 F.2d 1233 (8th Cir., 1970), *cert. denied*, 400 U.S. 852 (1970) 7, 8

STATUTES

Securities and Exchange Act of 1934, Section 9, 15 U.S.C., Section 78i(e) 10, 19
Securities and Exchange Act of 1934, Section 10(b), 15 U.S.C., Section 78j(b) 2
Securities and Exchange Act of 1934, Section 16(b), 15 U.S.C., Section 78p(b) 10, 19
Securities and Exchange Act of 1934, Section 18, 15 U.S.C., Section 78r(c) 10, 19
Securities and Exchange Act of 1934, Section 27, 15 U.S.C., Section 78aa 4, 18
Securities and Exchange Act of 1934, Section 29(b), 15 U.S.C., Section 78cc(b) 10, 19
Securities Act of 1933, Section 11, 15 U.S.C., Section 77k 10, 19
Securities Act of 1933, Section 12(2), 15 U.S.C., Section 77l 10, 19
Securities Act of 1933, Section 13, 15 U.S.C., Section 77m 10
Securities Act of 1933, Section 17a, 15 U.S.C., Section 77q(a) 9, 13
Securities and Exchange Act of 1934, Section 10(b), 15 U.S.C., Section 78j(b), Rule 10b-5, 17 C.F.R., Section 240.10b-5 ..... 2, 3, 5, 6, 7, 8, 9, 13, 14, 16, 19, 20
Federal Rule of Civil Procedure 12(b)(6) 4

Ohio Revised Code, Sections:
1707.01 ..... 3, 14
1707.40 3
1707.41 ..... 3, 15
1707.42 3
1707.43 ..... 3, 4, 15, 20
1707.44 ..... 3, 14, 15
Ohio Revised Code, Section 2305.07 6
Ohio Revised Code, Section 2305.09 ..... 3, 4, 5, 6

OTHER AUTHORITIES

A. Bromberg, *Securities Laws: Fraud—SEC Rule 10b-5*, Section 2.5(1), at 41-42 n. 105 (1969) 8
Schulman, *Statutes of Limitation in 10b-5 Actions: Complication Added to Confusion*, 13 Wayne L. Rev. 635 (1967) 18, 19
Israels, Book Rev. 77 Yale L.J. 1585, 1591-92 (1968) 18
VI L. Loss, SECURITIES REGULATIONS, at 3898-3900 (2d ed. 1961) 18

In the Supreme Court of the United States

OCTOBER TERM, 1976

No. .....

KOEHLER MANAGEMENT CORP., GERALD KOEHLER, ROGER BENHAM, WILLIAM J. EISENHAUER, PAUL M. GILLMOR, MARTIN A. JANIS, ROBERT B. JOHNSTON, RAY W. MOLDER, ALFRED E. RHODEN, M.D., GILBERT H. SIEGEL, RAY L. VISCHER, ESTATE OF JOSEPH A. SCHUSTER, DECEASED,

Petitioners,

vs.

CHARLES NICKELS and MARGARET NICKELS on Behalf of Themselves and All Other Shareholders of Koehler Management Corporation,

Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

To the Honorable, the Chief Justice and Associate Justices of the Supreme Court of the United States:

Koehler Management Corporation, Gerald Koehler, Roger Benham, William J. Eisenhauer, Paul M. Gillmor, Martin A. Janis, Robert B. Johnston, Ray W. Molder, Alfred E. Rhoden, M.D., Gilbert H. Siegel, Ray L. Vischer, Estate of Joseph A. Schuster, Deceased, the Petitioners herein, pray that a Writ of Certiorari issue to review the judgment of the United States Court of Appeals for the Sixth Circuit entered in the above entitled case on September 2, 1976.

OPINIONS BELOW

The Opinion of the Circuit Court of Appeals for the Sixth Circuit is reported in 541 F.2d 611 (6th Cir., 1976), and is printed in the Appendix, *infra*, page A1. The Opinion and Order of the United States District Court for the Northern District of Ohio, Western Division, CCH Federal Security Law Reporter Transfer Binder 75-76 decision ¶ 95,264, and is printed in the Appendix, *infra*, page A17.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on September 2, 1976. The jurisdiction of the Court is invoked under 28 U.S.C., Section 1254(1).

QUESTION PRESENTED FOR REVIEW

Should not the Sixth Circuit Court of Appeals in selecting the state statute of limitations to be applied to actions brought under Section 10(b) and Rule 10b-5 look to the statute of limitations contained in state Blue Sky Laws as have the Fifth, Seventh, and Eighth Circuit Courts of Appeal rather than applying a statute of limitations found in the general common law fraud section of the state Code?

STATUTES AND RULES INVOLVED

This case involves Section 10(b) of the Securities Exchange Act of 1934 (hereinafter "the 1934 Act"), 15 U.S.C., Section 78j(b), and Rule 10b-5 promulgated by the Se-

curities and Exchange Commission (hereinafter "SEC"), 17 C.F.R. 240.10b-5, the Ohio Securities Laws, O.R.C., Sections 1707.01, 1707.40, 1707.41, 1707.42, 1707.43, and 1707.44, and the Ohio statute dealing with the Statute of Limitations for common law fraud, O.R.C., Section 2305.09. All of these are reprinted in pertinent part in the Appendix, *infra*, pp. A27-A38.

STATEMENT OF THE CASE

1. Factual Background

The present action was filed on August 2, 1974, in the United States District Court for the Northern District of Ohio, Western Division. The Complaint set forth allegations under which a right to relief was claimed under Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 promulgated thereunder. Plaintiffs claimed that they and the class of shareholders they seek to represent suffered damages as the result of material, false, and misleading statements in the failure by Defendants to disclose material facts in the merger of two corporations, American Insurance Management Corporation (which changed its name to Koehler Management Corporation on the date of the merger) and Ohio Indiana Mutual Corporation (hereinafter "OIM"). The resulting corporation was known as Koehler Management Corporation (hereinafter "KMC"). Plaintiffs claimed that Defendants, who were directors of KMC at the time of the merger, failed to disclose to the shareholders the following facts, which are alleged the Defendants knew or should have known:

> OIM had loaned Defendant, Koehler, who was President of both OIM and KMC at the time, in excess of $590,000.00;

There was insufficient security in reserve for the loan;

The loan constituted a major asset of OIM; and

The loan was of doubtful collectibility and had, therefore, weakened OIM.

The Plaintiffs further alleged that the above information was not communicated to them and despite Defendants' knowledge of these facts the Defendants approved the merger of the two corporations and recommended shareholder approval. The merger was approved on May 8, 1970. The Plaintiffs further alleged that they did not discover the purported fraudulent acts until sometime in January, 1971, and that when the public learned of the loan the value of the Koehler stock dropped from $12.00 per share to $.60 per share.

2. Proceedings Below

Jurisdiction of the District Court was invoked under Section 27 of the 1934 Act, 15 U.S.C., Section 78aa. In the District Court all Defendants either filed or concurred in a Motion to Dismiss pursuant to Federal Rule of Civil Procedure 12(b)(6) on the grounds that the Complaint had not been timely filed and was barred by the applicable Ohio statute of limitations. The District Court in an Opinion and Order entered March 27, 1975, sustained Defendants' Motion to Dismiss finding that the state statute of limitations which best effectuates the Federal policy underlying the Federal securities laws was to be found in Ohio's Blue Sky Laws, Ohio Revised Code, Section 1707.43. This section provides a limitation of two years from the date of the act or omission complained of rather than four years from the discovery of such act or omission as set forth in the general statute of limitations governing common law fraud, Ohio Revised Code, Section 2305.09.

Thereafter, Plaintiffs perfected an appeal to the Sixth Circuit. This appeal was consolidated with the case of *McIntyre* v. *The First National Bank of Cincinnati,* (Sixth Circuit No. 75-2200), because both cases presented identical issues. The Sixth Circuit reversed the judgment of the District Court in the within case finding that the four year period of limitation in Ohio Rev. Code 2305.09 should be adopted because it best effectuated the policies of the Federal securities laws.

REASONS FOR GRANTING THIS WRIT

I. The Sixth Circuit's Application of the Four Year State Statute of Limitations Governing Common Law Fraud Actions Instead of the Two Year State Blue Sky Statute of Limitations Has Created a Direct Conflict With Recent Decisions of the Fourth, Fifth, Seventh, and Eighth Circuits Regarding the Applicable State Statute of Limitations for Implied Rights Under the Federal Securities Laws.

Section 10(b) of the Securities and Exchange Act of 1934, 15 U.S.C., Section 78j(b), and Rule 10b-5, 17 C.F.R., Section 240.10b-5 promulgated thereunder have no federal statute of limitations. As a result, the federal courts have applied the most appropriate state statute of limitations of the state in which the cause of action arose. *United Auto Workers* v. *Hoosier Cardinal Corp.*, 383 U.S. 696, 16 L.Ed.2d 192 (1966); *Campbell* v. *City of Haverhill,* 155 U.S. 610, 39 L.Ed. 280 (1895).

The task of the federal courts in determining the most appropriate state statute of limitations is governed by the so-called "resemblance test" as set forth in *Charney* v. *Thomas*, 372 F.2d 97, 100 (6th Cir., 1967), where the court stated:

"In such cases the Federal Courts must choose among the several state statutes of limitation and apply that one which best effectuates the federal policy at issue."

Before deciding the present case the Sixth Circuit had never been faced with the precise question here involved, i.e., in the choice in an action under Section 10 (b) and Rule 10b-5 brought in Ohio between the statute of limitations contained in the Ohio blue sky laws and the general statute of limitations for fraud.

Charney, supra, decided in 1967, involved a choice between a limitations period contained in Michigan's blue sky laws and that state's general fraud statute of limitations. The Court applied the state fraud limitations period, but in so doing conceded that:

"Although in some cases the local Blue Sky Law might be the more appropriate point of reference, in the present case the Michigan law contains no provision similar to section 10(b) of the federal law. Thus, the normal six-year period of M. S. A. §27A.5813 [for fraud] should apply despite the fact that actions under section 10(b) are not exactly the same as common law fraud actions." *Charney, supra,* 372 F.2d at 100.

Connelly v. *Balkwill,* 174 F. Supp. 49 (N.D. Ohio, 1959), *aff'd per curiam,* 279 F.2d 685 (6th Cir., 1960), cannot be cited as authority for the proposition that the Ohio fraud limitations period must be applied in a 10b-5 action. In *Connelly,* the Court was presented with the question of whether Ohio Revised Code Section 2305.07 (providing a six-year period of limitations applicable in actions based upon a liability created by statute) or Section 2305.09 (four-year fraud period) controlled a cause of action under Section 10(b) of the Securities and Exchange

Act of 1934 and Rule 10b-5 thereunder. The District Court adopted the shorter four-year statute, thus barring the claim and the Court of Appeals affirmed. Neither Court considered the question of whether a limitations period found in Ohio's blue sky laws would best effectuate the federal policy, and its holding cannot be construed to decide that it should not apply.

The Sixth Circuit conceded that the precise issue involved had not previously been considered in that Circuit but went on to hold that the common law of fraud is sufficiently similar to case law developing under Section 10(b) and Rule 10b-5 that Federal policy would be best served by the "continued" application of the four year limitation period approved in *Connelly* v. *Balkwill, supra.* (Appendix, p. A5). Thus, the Court on the one hand found there were no precedents within the Circuit upon which they could rely, and on the other hand, pointed to the *Connelly* case in calling for a "continued" application of a four year statute of limitations in 10b-5 actions.

In *Connelly* and *Charney,* the Court noted that as of that time (1960 and 1967, respectively) no case had applied other than a state general fraud statute of limitations in a 10b-5 action; but as the District Court in the present case stated: "since then the reverse is nearly true." (Appendix, p. A19) See, *Hudak* v. *Economic Research Analysts, Inc.,* 499 F.2d 996 (5th Cir., 1974); *Parrent* v. *Midwest Rug Mills, Inc.,* 455 F.2d 123 (7th Cir., 1972); *Vanderboom* v. *Sexton,* 422 F.2d 1233 (8th Cir., 1970), *cert. denied,* 400 U.S. 852 (1970).

The Eighth Circuit in *Vanderboom, supra,* was the first Court to look to a body of state law, which had been enacted for the specific purpose of dealing on the state level with the same type of conduct covered by the Federal securities laws. In *Vanderboom* the Court

dismissed the contention that no other Federal case had applied the Blue Sky statute of limitations by stating:

> "While the appellants contend that no federal case has applied a short blue-sky statute of limitations, it appears this ordinarily would be the most reasonable and logical type of statute to apply to essentially what might be termed an 'implied federal blue-sky' type of statutory action." [Citations omitted]. *Vanderboom, supra,* 422 F.2d at 1237.

The Court then compared the Arkansas blue sky statute with Rule 10b-5. Despite the fact that it was "evident" that the two were not identical, the Court found a "commonality of purpose" and a similarity of interpretation which mandated the selection of the blue sky laws as the appropriate statute of limitations.

The Seventh Circuit Court of Appeals has taken the same approach by adopting the three year limitations period established by the Illinois Securities Law for actions under Section 10(b) and Rule 10b-5. *Parrent* v. *Midwest Rug Mills, Inc.,* 455 F.2d 123 (7th Cir., 1972). *Parrent* specifically rejected the application of the state general fraud statute of limitations.

> "It is clear that under the resemblance test the three year limitation in Section 13, subd. D of the Illinois Securities Law . . . applies to the 10b-5 actions. . . ." [*Citing Bromberg, Securities Laws: Fraud —SEC Rule 10b-5,* Section 2.5(1), at 41-42 n. 105 (1969)].
>
> "The three year limitation is also closer to the express limitation periods in the various sections of the federal act, ... Furthermore, logic dictates selection of the three year Illinois limitation as tending more toward an orderly development of law, than

> reaching into a different Illinois Act [for fraud] for the appropriate limitation." *Parrent, supra,* 455 F.2d at p. 127.

After considering the holding of the Sixth Circuit in *Charney,* the Seventh Circuit distinguished it on the ground that Michigan had no blue sky provision like Section 10(b) or Rule 10b-5. The same does not hold true in relation to the Ohio Securities laws.

The Fifth Circuit in *Hudak* v. *Economic Research Analysts, Inc.,* 499 F.2d 996 (5th Cir., 1974), *cert. denied,* 419 U.S. 1122 (1975), has followed the example of the Seventh and Eighth Circuits by holding that the limitations period set forth in local blue sky laws should be applied in an action under Section 10(b). The Court noted the similarity in language and interpretation of the Federal and State acts and what is referred to as the "congruence" between the State and Federal schemes:

> "Defendants contend, however, that Section 517.301(1) of the Florida blue sky laws, which deals with fraudulent transactions in securities, more nearly embodies the policies behind section 10(b) and the related Rule 10b-5 and that the two-year limitations period applicable in suits brought to rescind sales conducted in violation of that statute would therefore govern a 10b-5 action in Florida. We find this argument persuasive." *Hudak, supra,* 499 F.2d at 999.

The case of *Newman* v. *Prior,* 518 F.2d 97 (4th Cir., 1975), involved an action under Section 17(a) of the Securities Act of 1933, 15 U.S.C., Section 77q(a) arising out of a fraudulent sale of securities. The case is relevant here because Section 17(a) of the 1933 Securities Act, like Section 10(b) of the 1934 Act, contains no federal statute of limitations. The *Newman* Court was thus faced

with the same issue as here involved with the same choice between state limitations periods, i.e., the general fraud limitation as contrasted with the limitation contained in the state blue sky law. In applying the statute of limitations found in Virginia's blue sky law, the Court stated:

> "Virginia's blue sky law, however, has a two-year period of limitations for actions arising out of the fraudulent sale of securities. Both the state statute and Section 17(a) proscribe the same conduct. In addition, the two-year period is closer to limitations on actions under other sections of the federal securities laws than the Virginia five-year period. We hold, therefore, that federal policy is best served by applying the state blue sky law's two-year statute of limitations to a suit involving the fraudulent sale of securities." (Citations omitted). *Newman, supra.*

As the Court noted, long limitations periods in private civil suits under the securities laws have not been favored by Congress. *Newman, supra,* 518 F.2d at 100 n. 4. Section 13 of the 1933 Act [15 U.S.C., Section 77m], limits actions for civil liabilities under Section 11 and Section 12(2) [15 U.S.C., Sections 77k and 77l] to one year after the violation should have been discovered up to a maximum of three years. The same holds true for actions brought under Sections 9, 18, and 29(b) of the Securities and Exchange Act of 1934 [15 U.S.C., Sections 78i(e), 78r(c), and 78cc(b)]. Actions under Section 16(b) of the 1934 Act [15 U.S.C., Section 78p(b)] are limited to two years after the event. The *Newman* Court viewed the short limitation periods under the federal securities laws as significant in holding that a two year period of limitations under state blue sky laws should be applied to an action under Section 17(a) of the 1933 Act.

The most recent pronouncement on the issue comes from the Second Circuit in the case of *Berry Petroleum Company* v. *Adams & Peck,* 518 F.2d 402 (2nd Cir., 1975). Although in *Berry* the result was the selection of a three year statute of limitations rather than a two year statute, the significance of the decision is that a Federal Court adopted a limitations period from the state regulatory scheme for securities transactions rather than an unrelated statute which developed without regard to the securities law.

In addition to these decisions by appellate courts, a host of district courts have reached the same conclusion. *E.g. Corey* v. *Bache & Co.,* 355 F. Supp. 1123 (S.D. W.Va., 1973) (Indiana two-year blue sky statute applied rather than six-year fraud statute); *Hitchcock* v. *deBruyne,* 377 F. Supp. 1403 (D. Conn., 1974) (two-year Connecticut blue sky statute applied over three-year tort statute); *Batchelor* v. *Legg & Co.,* 52 F.R.D. 553 (D. Md., 1971) (two-year Maryland blue sky statute adopted without discussion); *Josef's of Palm Beach, Inc.* v. *Southern Investment Co.,* 349 F. Supp. 1057, 1060 (S.D. Fla., 1972) (Florida's two-year blue sky statute "natural and logical choice" over three-year fraud statute); *Kramer* v. *Loewi & Co.,* 357 F. Supp. 83, 87 (E.D. Wis., 1973) (Wisconsin's one-year blue sky limitation "closer to the express limitations periods in other sections of the Securities and Exchange Act than is the six-year limitations period for fraud").

The only recent exception to this trend is the Ninth Circuit decision in *United California Bank* v. *Salik,* 481 F.2d 1012 (9th Cir., 1973), *cert. denied,* 414 U.S. 1004 (1973). The Ninth Circuit in *Salik,* however, relied on prior decisions of that Court in applying a local fraud statute of limitations, a situation not found in the Sixth Circuit

in the present case. The Ninth Circuit was concerned about the uncertainty that might result from a change of position and the possible harm that might result from reliance on its previous decisions and felt compelled to follow its earlier rulings. The Ninth Circuit recognized, however, that its answer was not "entirely satisfactory" and it seemed to be looking to Congress for relief. It must be noted that the Sixth Circuit in the present case appeared to rely heavily upon the same type of logic when it stated:

> "We conclude that the common law fraud is sufficiently similar to the case law developing under Section 10(b) and Rule 10b-5 that Federal policy will best be served by the *continued* application of the four year limitation period that we approved in *Connelly* v. *Balkwill, supra.* In *IDS Progressive*, we held that we should not change the limitation period applicable to 10b-5 actions without 'good cause' because to do otherwise adds 'unnecessary uncertainty to the prosecution of Federal claims under Section 10b-5.' 533 F.2d at 343." [Emphasis supplied by the Court]. (Appendix, pp. A15-A16).

The Court, therefore, relied upon the *Connelly* case even though it conceded in another portion of its Opinion that that case was not dispositive of the precise issue involved. Petitioners submit that such reliance on *Connelly* is totally misplaced.

II. Under the Resemblance Test, Ohio Revised Code Section 1707.43 Best Effectuates Federal Policy.

The Sixth Circuit acknowledged the trend in other Circuits to apply statutes of limitations found in blue sky laws to implied rights of action under federal securities laws. The Court, nevertheless, applied a common law

fraud statute of limitations for the reasons that "Federal policy will be best served by the continued application of the four year limitation period approved in *Connelly* v. *Balkwill*" and "the broad remedial purposes of the federal securities acts are best served by a longer, not a shorter, statute of limitations." (Appendix, p. A16). The Court determined that a choice between the Ohio common law fraud and its blue sky statutes could not be made under the resemblance test since both were similar to a 10b-5 action but neither was identical. Petitioners concede that Ohio's blue sky laws are not identical with Section 10(b) and Rule 10b-5, but they believe the resemblance is much closer than is common law fraud.

In choosing which statute to apply, it is necessary to consider the entire Ohio Securities Act. There is no necessity that the local blue sky law contain a carbon copy of Rule 10b-5 if, in its entirety, it covers common ground, is intended to curb similar types of misconduct, and has not been interpreted in a manner totally inconsistent with the interpretation of the federal securities laws. Obviously, if the blue sky law is limited to the establishment of a regulatory agency and the promulgation of rules relating to the registration of securities for sale, then it does not sufficiently resemble the antifraud provisions of the federal securities law to pass the resemblance test. On the other hand, if despite a different format, the blue sky law is part of a regulatory scheme intended to protect the innocent purchaser of securities from fraud, artifice and deceit in a manner that extends beyond the common law remedies, then it would seem more reasonable and logical to adopt the blue sky statute of limitation.

It is evident that Chapter 1707 contains no provisions that are identical to section 17(a) of the 1933 Act or section 10(b) of the 1934 Act. However, a close examina-

tion of the Ohio law reveals a remarkable similarity in the purpose and scope between the Ohio and the federal statutes. Like the Florida statutes considered in *Hudak* v. *Economic Research Analysts, Inc., supra,* 499 F.2d at 999, the antifraud provisions of the Ohio law "address the problems of false and misleading communications involving the sale of securities. . . ."

Section 1707.44(G) provides that no one shall knowingly engage in any act or practice defined as fraudulent. "Fraudulent acts" and "fraudulent practices" are defined by Section 1707.01(J) in terms which echo the phraseology of section 17a and Rule 10b-5.

§ 1707.01

> (J) "Fraud", "fraudulent acts," "fraudulent practices," and "fraudulent transactions" mean anything recognized on or after July 22, 1929, as such in courts of law or equity; any device, scheme, or artifice to defraud or to obtain money or property by means of any false pretense, representation, or promise; any fictitious or pretended purchase or sale of securities; and any act, practice, transaction, or course of business relating to the sale of securities which is fraudulent or which has operated or would operate as a fraud upon the purchaser.

In addition Ohio Revised Code Section 1707.44(B)(4) provides:

> No person shall knowingly make or cause to be made any false representation concerning any material and relevant fact, in any oral statement or in any prospectus, circular, description, application, or written statement for any of the following purposes:
>
> * * *
>
> (4) Selling any securities in this state.

Victims of such fraudulent activities are entitled to rescission of the sale (1707.43) and in some instances damages (1707.41).

This Court recently determined that a private cause of action for damages under Section 10(b) and Rule 10b-5 will not lie in the absence of any allegation of scienter, i.e., intent to deceive, manipulate, or defraud. *Ernst & Ernst* v. *Hochfelder,* ..... U.S. ....., 47 L.Ed.2d 668, 96 S.Ct. ..... (March 30, 1976). The Ohio securities laws follow this holding. For example, Section 1707.43, the broad remedy provision of the blue sky laws, provides that "[e]very sale or contract of sale made in violation of 1707.01 to 1707.45, inclusive, of the Revised Code is voidable at the election of the purchaser." When this Section is read in conjunction with Section 1707.44, forbidding "knowing" violations, it is clear that Ohio requires intent to defraud but does not necessarily require the element of reliance in order to effectuate rescission. On the other hand, Section 1707.41 requires reliance in order to establish a cause of action for damages but shifts the burden of proof relating to knowledge from the Plaintiff to the Defendant. *See, also, Crane* v. *Courtright,* 2 O.App. 2d 125, 206 N.E.2d 913 (Franklin Co., 1964). In *Affiliated Ute Citizens* v. *United States,* 406 U.S. 128 (1972), this Court held in a situation involving nondisclosure that proof of reliance was not necessary for recovery. On the other hand, in common law fraud suits Ohio does not require the Plaintiff to show that the Defendant knowingly made the misrepresentation upon which Plaintiff relied. *Beamer* v. *Feick,* 113 O.App. 264, 177 N.E.2d 691 (Erie Co., 1960).

As Judge Walinski observed in the present case, when the resemblance test is applied "it is at once apparent"

that an action under Rule 10b-5 bears a closer resemblance to an action under the Ohio Securities Act than to an action in common law fraud and deceit. This similarity is hardly surprising. The Ohio law is part of a special statutory scheme dealing with the same subject and enacted for the same reasons as the federal securities acts. In view of this identity of purpose and subject matter, and the close resemblance of the actual provisions, there is no reason to go outside the securities law to select a period of limitations from a statute totally unrelated to securities law. The lack of any rational basis for applying a common law fraud statute of limitation is further emphasized by the fact that the common law period is longer than either the state or federal legislatures thought appropriate when they were considering and adopting laws specifically intended to regulate securities transactions. There is no rational reason for assuming that the policy underlying the state securities laws is any different from that which underlies the federal statutes or that either legislature did not consider and weigh the welfare of its citizens when they both determined that a period of limitations shorter than that employed for common law fraud actions would better effectuate the policy being implemented in their scheme of securities regulations.

III. The Federal Policy Underlying the Implied Remedies Found in Section 10(b) and Section 17(a) Would Be Better Effectuated by Application of the Statutes of Limitation Found in Other Federal Securities Provisions, Rather Than Those That Apply to State Common Law Fraud.

A. The Application of State Statutes of Limitation Results in Unfair Distinctions Between Plaintiffs in Different States.

A review of the many federal cases in which courts have applied state limitation periods to implied rights of action under the federal securities laws illuminates the hodge-podge of statutes that have been employed. A cross-section of decisions, some of which have been implicitly or expressly overruled, reveals the variety of limitations that have been applied to the same statutes. *Denny* v. *Performance Systems, Inc.*, [1971-72 Transfer Binder] CCH Fed. Sec. L. Rep. ¶ 93,387 (M.D. Tenn., 1971) (Tennessee ten-year statute); *Saylor* v. *Lindsley*, 391 F.2d 965 (2d Cir., 1968), and *Fischman* v. *Raytheon Manufacturing Co.*, 188 F.2d 783 (2d Cir., 1951) (New York six-year statute); *Morgan* v. *Koch*, 419 F.2d 993 (7th Cir., 1969) (Indiana six-year statute); *Butterman* v. *Steiner*, 343 F.2d 519 (7th Cir., 1965) (Illinois five-year statute); *Parrent* v. *Midwest Rug Mills, Inc.*, 455 F.2d 123 (7th Cir., 1972) (Illinois three-year statute); *Dudley* v. *Southeastern Factor and Finance Corp.*, 57 F.R.D. 177 (N.D. Ga., 1972) (Georgia four-year statute); *Aboussie* v. *Aboussie*, 441 F.2d 150 (5th Cir., 1971) (Texas two-year statute); *Bailes* v. *Colonial Press, Inc.*, 444 F.2d 1241 (5th Cir., 1971) (Alabama one-year statute).

The practice of adopting the state limitation period which best effectuates federal policy has obviously led to institutionalized differences between forums. The plain-

tiff who can wait only a year in Alabama might find a claim identical to his litigated nine years later by another plaintiff across the state line in Tennessee. In actions where class actions are a routine way of pleading, forum shopping is encouraged by such ragged periods of limitation.

The problem is compounded by the venue provisions of section 27 of the 1934 Act, 15 U.S.C. § 78aa, which permits a plaintiff to bring an action in any district where: (1) an act or transaction constituting the violation occurred, (2) the defendant is found, (3) the defendant is an inhabitant, (4) or the defendant transacts business. A plaintiff should not be able to manipulate the broad choice of forums by statute-of-limitations shopping.

B. Federal Policy Can Best Be Determined by Examining the Statutes of Limitation Adopted by Congress for Express Rights of Action Under the Securities Laws.

The surest way to effectuate federal policy is to look at what Congress provided when it considered the problems of limitation periods under the federal securities laws. Such an approach has been suggested by numerous commentators. Schulman, *Statutes of Limitation in 10b-5 Actions: Complication Added to Confusion*, 13 Wayne L. Rev. 635 (1967); Israels, Book Rev., 77 Yale L.J. 1585, 1591-92 (1968); VI L. Loss, SECURITIES REGULATIONS, at 3898-3900 (2d ed. 1961).

A review of the 1933 and 1934 Acts indicates that Congress considered that the policy of the United States in the securities area would be best served by the relatively short period of limitation of one year from discovery with a maximum of three years from the incident. This was the period that Congress chose to apply to the express

rights of action conferred by the 1933 and 1934 Acts, including claims for fraud. Thus, suits under sections 11, 12(1) and 12(2) of the 1933 Act are governed by the one-year-from-discovery, three-year maximum, limitation period of section 13 of the Act. Suits under the express liability provisions of the 1934 Act are governed by a similar one-year-from-discovery, three-year maximum, limitation, found in sections 9(e), 18(c) and 29(b). The express liability provisions governed by these sections cover diverse concepts of liability and proscribe a broad variety of activities. All, however, are governed by the same limitation period: one year from discovery and a maximum of three years. The only statute which disrupts this pattern is found in section 16(b), which provides a two-year period. That section, however, is intended to be prophylactic rather than remedial; in any event it reemphasizes the federal policy of relatively short periods of limitation in the area of securities laws. Schulman, *supra*, 637-38.

The consistent pattern throughout the federal securities laws is indicative that Congress considered a uniform one-year-from-discovery statute of limitations to be an integral part of the federal regulatory scheme. Application of state statutes of limitations contradicts rather than carries out this federal policy. The borrowing of state statutes creates longer periods of limitation for implied actions than exist under express remedy provisions and produces inconsistent results from forum-to-forum.

To effectuate a logical and orderly development of the law under Section 10(b) and Rule 10b-5, Courts should not continue to borrow state statutes of limitations in view of the repeated and consistent pronouncements by Congress that federal policy favors a one-year-from-discovery statute of limitations for federal claims alleging securities fraud. Even if it is determined that state statutes

of limitations should apply in 10b-5 actions, utilizing the resemblance test, shorter limitation periods should be favored because of this federal policy. In the instant case, it is the two year period of Ohio Revised Code, Section 1707.43, contained in Ohio's blue sky laws, which best effectuates federal policy.

CONCLUSION

For the foregoing reasons, this Petition for a Writ of Certiorari should be granted to allow this Court to resolve the conflict among the Circuits on the important and recurring Federal questions presented herein.

Respectfully submitted,

STANLEY GOODMAN
RONALD K. RYCHENER
GOODMAN & GOODMAN CO., L.P.A.
1016 Fourth & Walnut Building
36 East Fourth Street
Cincinnati, Ohio 45202
(513) 621-1503
Attorneys for Petitioners

APPENDIX

Nos. 75-1684, 75-2200

UNITED STATES COURT OF APPEALS
FOR THE SIXTH CIRCUIT

No. 75-1684

CHARLES NICKELS, MARGARET NICKELS, on behalf of themselves and all other shareholders of Koehler Management Corporation, *Plaintiffs-Appellants*,

v.

KOEHLER MANAGEMENT CORP., GERALD KOEHLER, ROGER BENHAM, WILLIAM J. EISENHAUER, PAUL M. GILLMOR, STANLEY GOODMAN, MARTIN A. JANIS, ROBERT B. JOHNSTON, RAY W. MOLDER, ALFRED E. RHODEN, M.D., GILBERT H. SIEGEL, RAY L. VISCHER, Estate of JOSEPH A. SCHUSTER, Dcd., *Defendants-Appellees*.

ON APPEAL from the United States District Court for the Northern District of Ohio, Western Division.

No. 75-2200

RHODA V. MCINTYRE, Individually and as a Representative of a Class, *Plaintiff-Appellee*,

v.

THE FIRST NATIONAL BANK OF CINCINNATI, Individually and as Agent, *Defendant-Appellant*.

ON APPEAL from the United States District Court for the Southern District of Ohio, Western Division.

Decided and Filed September 2, 1976.

Before: PECK, MCCREE, and MILLER,* Circuit Judges

*Judge Miller died April 12, 1976 and did not participate in this opinion.

McCree, Circuit Judge. We consolidated these two appeals because they present the same question: what statute of limitations should be applied in an action in a United States District Court in Ohio based upon Rule 10b-5, § 10(b) of the Securities Exchange Act of 1934, and § 17(a) of the Securities Act of 1933. In case No. 75-2200, *McIntyre* v. *The First National Bank of Cincinnati*, the District Court for the Southern District of Ohio, Western Division, applied Ohio's four year statute of limitations for general fraud, Ohio Rev. Code 2305.09. In case No. 75-1684, *Nickels* v. *Koehler Management Corp.*, the District Court for the Northern District of Ohio, Western Division, applied the Ohio two year blue sky period of limitations, Ohio Rev. Code 1707.43.

We hold that the four year period of limitation in Ohio Rev. Code 2305.09 should be adopted because it best effectuates the policies of the federal securities laws.

The plaintiff in *McIntyre* is a former shareholder in the Verkamp Corporation, which was acquired by KDI Corporation and KDI Verkamp pursuant to a merger agreement approved by the Verkamp shareholders. McIntyre alleged that the approval of the merger was fraudulently induced by the KDI defendants, and that the merger agreement provided for the exchange of 27 shares of KDI stock, which had a value of less than $2 per share, for each share of Verkamp stock, which had a value of $900 per share. Another portion of the original complaint charged the First National Bank with a transfer in defraud of creditors and a fraudulent conveyance both arising from KDI's pledge to the bank of the shares and assets of the former Verkamp corporation after the merger. In a second amended complaint, McIntyre also alleged that First National controlled, aided and abetted, and participated in the fraudulent acquisition of Verkamp as security

for KDI's debts to First National and a group of banks represented by First National. The bank contended that the new claims in the second amended complaint did not arise out of the transaction set forth in the original complaint, and that they were barred by the two year statute of limitations in the state blue sky law.[1] The district court granted McIntyre's motion for leave to file the second amended complaint, holding that the four year general fraud limitation, Ohio Rev. Code 2305.09, applied. The district court certified the question of the proper limitation period under 28 U.S.C. § 1292(b), and we granted leave for an interlocutory appeal.

The plaintiffs in the second case, *Nickels*, are stockholders in the Koehler Management Corporation. The allegations of the complaint are as follows. In 1970, pursuant to the recommendation of their board of directors, the stockholders of Koehler approved a merger with Ohio Indiana Mutual Corporation. Several Koehler directors were also directors of Ohio Indiana. At the time they urged approval of the merger, the Koehler directors knew or should have known that in 1969, Ohio Indiana had loaned $590,000, with no collateral, to Gerald Koehler (who was at that time president of both Koehler and Ohio Indiana), that the loan was still outstanding, and that it was uncollectible. The complaint alleges that when the public learned of the loan, the value of the Koehler

---

1. The only claim against First National in the original complaint arose out of an alleged transfer in defraud of creditors, which took place after the merger. The second amended complaint included, for the first time, the claim that First National was also liable for the injury suffered by the plaintiffs as a result of the merger, on the theory First National had become a controlling person and an aider and abettor. The district court held that if the two year statute of limitations were applicable, the new claims of First National's liability relating to the merger would not relate back because they did not arise out of the same transaction set forth in the complaint, F.R. Civ.P. 15(c).

stock dropped from $12.00 per share to $.60 per share. The district court sustained the defendants' motion to dismiss on the grounds that the two year statute of limitations in the Ohio blue sky law barred the cause of action.[2] Plaintiffs appeal from that order.

Neither § 10(b) of the 1934 Act, nor § 17(a) of the 1933 Act contains a period of limitations, and there is no general federal statute of limitations. Accordingly, we held in a § 10(b) case that "'[T]he Federal Courts must choose among the several state statutes of limitations and apply that one which best effectuates the federal policy at issue.'" *I.D.S. Progressive Fund, Inc.* v. *First of Michigan Corp.*, 533 F.2d 340, 342 (6th Cir. 1976), *quoting Charney* v. *Thomas*, 372 F.2d 97, 100 (6th Cir. 1967). This view was approved recently by the Supreme Court in *Ernst & Ernst* v. *Hochfelder*, 44 U.S.L.W. 4451, 4459 n.29 (March 30, 1976):

> Since no statute of limitations is provided for civil actions under § 10(b), the law of limitations of the forum state is followed as in other cases of judicially implied remedies. *See Holmberg* v. *Armbrecht*, 327 U.S. 392, 395 (1946), and cases cited therein.

---

2. The district judge distinguished *Toledo Trust Co.* v. *Nye*, Civ. No. C 72-281 (W.D. Ohio, N.Div., Mem. Opinion, February 25, 1975), in which another judge from the Northern District of Ohio applied the four year limitation period following *Charney, et al.* The *Nickels* court held that *Toledo Trust* was distinguishable because there the plaintiff was the personal representative of a deceased seller of securities. Since Ohio's blue sky law provided no remedy for a defrauded seller, his only remedy under state law was an action for fraud. Accordingly, the fraud action might more closely resemble *his* suit. Moreover, since the action was filed only two years and five days after the discovery of the fraud, the district judge in *Nickels* viewed the *Toledo Trust* case "as an application of the 'flexibility' commanded by *Affiliated Ute Citizens, supra*, and the equity notions . . . which lie at the heart of a federal court's use of a state statute of limitations in an action where the rights and liabilities are created by federal law."

The question whether the *Ohio* blue sky period of limitations or fraud period would better implement the federal policies underlying Rule 10b-5 and §§ 10(b) and 17(a) has not previously been considered by our court. However, in *Connelly* v. *Balkwill*, 279 F.2d 685 (6th Cir. 1960), we affirmed, without discussion, a determination by the District Court for the Northern District of Ohio that the four year fraud period should be applied in preference to the six year limitation period for actions based upon a liability created by statute, Ohio Rev. Code 2305.07. The two year blue sky limitation period was not considered. The district court opinion, reported at 174 F. Supp. 49 (N.D. Ohio 1959), focused on the fact that § 10(b) and Rule 10b-5 did not create a new kind of liability, but rather incorporated into statute and rule the common law fraud action. Accordingly, the court applied the six year fraud limitation. It did not discuss the applicability of Ohio Rev. Code 1707.43, the two year blue sky limitation. The district court also discussed the resemblance between the Ohio law of fraud and 10b-5 in connection with the defendants' claim that res judicata barred the 10b-5 action because plaintiffs had already been denied recovery in a state fraud action. The court held that "this [10b-5] case is based on a cause of action no different from the cause of action upon which plaintiffs sought recovery in the previous [fraud] action." It found that

> Ohio must be assigned a place among those "more enlightened jurisdictions" where *the duty to disclose material facts is as broad and exacting as the duty of disclosure defined by Rule X 10b-5.* 174 F. Supp. 60. [Emphasis added.]

Then, in *Charney* v. *Thomas*, 372 F.2d 97 (6th Cir. 1967) we were presented with a choice between applying the six year Michigan limitation for general fraud and

the two year limitation in the state blue sky law. The plaintiff alleged fraudulent misrepresentation in violation of § 10 of the 1934 Act. We held that the six year limitation for fraud would best promote federal policy because the Michigan statute did not contain a provision similar to 10(b).

Most recently in *I.D.S. Progressive Fund, Inc.* v. *First of Michigan Corp.*, 533 F.2d 340 (6th Cir. 1976), we rejected the contention that we ought to apply the new Michigan blue sky limitation contained in the Uniform Securities Act, which was adopted in place of the earlier blue sky law considered in *Charney*. We held that "[f]or us to change the applicable limitation period without good cause would add an unnecessary uncertainty to the prosecution of federal claims under Section 10(b)." 533 F.2d 343. Additionally, we observed that " 'the broad remedial purposes of the federal securities laws are best served by a longer, not a shorter statute of limitations.' " 533 F.2d 344, *quoting United California Bank* v. *Salik*, 481 F.2d 1012 (9th Cir.), *cert. denied*, 414 U.S. 1004 (1973).

Although we have not applied a state blue sky limitation in any of the cases before us, we are aware that other circuits have applied similar blue sky limitations periods in fraud cases based upon 10b-5, and sections 10(b) and 17(a). *Newman* v. *Prior*, 518 F.2d 97 (4th Cir. 1975), *Hudak* v. *Economic Research Analysts, Inc.*, 499 F.2d 996 (5th Cir. 1974), *cert. denied*, 419 U.S. 1122 (1975), *Parrent* v. *Midwest Rug Mills, Inc.*, 455 F.2d 123 (7th Cir. 1972), *Vanderboom* v. *Sexton*, 422 F.2d 1233 (8th Cir. 1970), *cert. denied*, 400 U.S. 852 (1970). In each of these cases, the court determined that the state blue sky law closely resembled the federal securities provisions. For example, in *Parrent*, the Seventh Circuit observed that the state blue sky law had a purpose similar to the 10b-5's purpose "of

protecting the 'uninformed, the ignorant, the gullible.' " 455 F.2d 126. The court determined "Except for the interstate elements in 10b-5, *Section 12 of the Illinois Securities Law . . . covers the same violations as 10b-5.*" 455 F.2d 127. [Emphasis added.] The court found it important that section 137.12 "so closely parallels 10b-5," and it concluded that the adoption of this section would best effectuate the federal policies in the suit. Similarly, in *Hudak*, the Fifth Circuit observed that "the present hesitant growth of the Florida blue sky law accurately tracks the development of federal securities regulation in this Circuit." 499 F.2d 1000. Most recently in *Newman* the court found that "[b]oth the state statute and 617(a) proscribe the same conduct." 518 F.2d 100.

The defendants in this consolidated appeal present several arguments for the application of periods of limitation that would bar plaintiffs' claims. First, they urge that we should fashion a uniform statute of limitations of one year from discovery, up to a maximum of three years, based upon the sections of the 1933 and 1934 Acts that create express liabilities with stated periods of limitations. 15 U.S.C. §§ 77m, 78i(e), 78r(c), and 78cc(b). They contend that a uniform federal standard is essential to prevent confusion and uncertainty. We decline, as we did in *IDS' Progressive*, to overrule our precedents fashioning the federal limitation period in 10b-5 actions after the state limitation that will best effectuate federal policy. Although a uniform federal period of limitation would prevent the anomaly of applying different limitations periods to plaintiffs who purchased or sold the same security but resided in different states, a single circuit cannot impose a pattern on the entire nation. Each circuit that has considered the question to date has applied a state period of limitation. Accordingly, at this late hour only the Congress or the Supreme Court can impose uniformity.

Neither has promulgated a federal limitation period, and the Supreme Court recently observed that "since no statute of limitations is provided under § 10(b), the law of the forum state is followed as in other cases of judicially implied remedies." *Ernst & Ernst*, 44 U.S.L.W. 4459 n.29. Moreover, the *Ernst* opinion provides no support for defendants' contention that a one year from discovery federal limitation period is necessary because longer state limitations contravene federal policy. The *Ernst* opinion observed, without disapproval:

> Although it is not always certain which state statute of limitations should be followed, such statutes of limitations usually are longer than the period provided under § 13.3 L. Loss, *supra*, at 1773-1774. 44 U.S.L.W. 4459 n.29.

Alternatively, defendants urge that if state law is to be applied, the shorter two year blue sky statute of limitations will best promote federal policies. In support of this claim, they present two arguments. In determining which state limitations period will best promote federal policies, the courts have tried to determine which state statute "bears the closest resemblance to the federal statute involved." *Vanderboom* v. *Sexton*, 422 F.2d 1237-1238. The defendants' first contention is that each of the state law causes of action that resembles the federal cause of action here—both blue sky *and* state common law securities fraud—is governed by the two year limitation in the blue sky statute. In the alternative, they contend that even if a state action for common law securities fraud is governed by the longer fraud limitation period, the blue sky cause of action resembles the 10b-5 cause of action more closely than does the state common law action for fraud.

Evaluation of these two arguments requires a close examination of the provisions of the blue sky statute. Sec-

tion 1707.43 is the general section creating the purchaser's remedies for an unlawful securities sale. It includes a two year limitation period. It provides:

> *Every sale or contract for sale made in violation of sections 1707.01 to 1707.45*, inclusive, of the Revised Code, is voidable at the election of the purchaser. The person making such sale or contract for sale, and every person who has participated in or aided the seller in any way in making such sale or contract for sale, are jointly and severally liable to such purchaser, in an action at law in any court of competent jurisdiction, upon tender to the seller in person or in open court of the securities sold or of the contract made, for the full amount paid by such purchaser and for all taxable court costs, unless the court determines that the violation did not materially affect the protection contemplated by the violated provision.
>
> *No action for the recovery of the purchase price as provided for in this section, and no other action for any recovery based upon or arising out of a sale or contract for sale made in violation of sections 1707.01 to 1707.45*, inclusive, of the Revised Code, *whether based upon contract or tort, and whether legal or equitable in nature, shall be brought after two years from the date of such sale or contract for sale.* [Emphasis added.]

Plaintiffs argue first that the language of 1707.43, read in conjunction with 1707.40, establishes that the Ohio legislature intended the two year limitation period to apply to *all* causes of action based upon fraud in the sale of securities. Section 1707.40 provides:

> Sections 1707.01 to 1707.45, inclusive, of the Revised Code create no new civil liabilities, and do not limit

> or restrict common law liabilities for deception or fraud other than as specified in sections 1707.41, 1707.42, and 1707.43 of the Revised Code, and there shall be no civil liabilities for noncompliance with orders, requirements, rules, or regulations made by the division of securities under sections 1707.19, 1707.20, and 1707.23 of the Revised Code.

They emphasize the statement in 1707.40 that the blue sky provisions "do not limit or restrict common law liability for deception or fraud *other than as specified in section . . . 1707.43. . . .*" [Emphasis added.] Accordingly, they reason that the two year limitation contained in 1707.43 *does* "limit or restrict common law liability for deception or fraud." This interpretation is supported by 1707.43, which makes the two year limit applicable to any action for

> *recovery based upon or arising out of a sale or contract for sale made in violation of section 1707.01 to 1707.45,* inclusive, of the Revised Code, *whether based upon contract or tort, and whether legal or equitable in nature. . . .* [Emphasis added.]

However, we do not agree that the two year limitation period in § 1707.43 was intended to apply to *all* cases of securities law fraud, including those based solely upon the common law of fraud. At the outset, we observe that the two other sections of the blue sky provisions creating liability have their own limitations periods. Ohio Rev. Code 1707.41 (liability of director of seller corporation, two years), Ohio Rev. Code 1707.42 (liability of advisor to seller, one year). But of greater significance is the fact that the Ohio legislature intended § 1707.43 to be given a common sense interpretation. It applies to cases where the plaintiff claims that his recovery is

"based upon" or "aris[es] out of" a violation of the blue sky provisions, whether the theory of damages is contract or tort, at law or equity. But § 1707.43 was not, we believe, intended to apply to actions in which the plaintiff does not expressly "base [his claim] upon" and does not contend that it "aris[es] out of" the blue sky law. And although plaintiffs argue that any sale that would constitute common law fraud would also violate the blue sky provisions, we have no authoritative construction by the Ohio courts that their blue sky law is intended to be co-extensive with their common law of fraud. As our discussion below will demonstrate, we do not view the common law of fraud and the blue sky provisions as identical.

This brings us to consideration of defendants' final argument, that the federal period of limitations should be the same as the two year blue sky limitation because the federal action more closely resembles the cause of action created by the blue sky statute. Accordingly, they contend that a two year statute of limitations will best promote federal policy.

It is difficult to determine whether the federal cause of action more closely resembles the action for common law fraud or the action created by the blue sky statute because the federal action has elements common to both, and also has features possessed by neither.

One difference is immediately apparent. The blue sky law provides a remedy only for a defrauded purchaser, and not for a defrauded seller. On the other hand, the action for common law fraud and the federal cause of action afford a remedy for a defrauded seller as well.

The Ohio blue sky statute, its common law action for fraud, and 10b-5 also differ in their treatment of re-

liance and scienter. The blue sky statute affords two contrasting remedies. Rescission is available for intentional misrepresentation without a showing of reliance, but otherwise damages can be recovered only where there has been reliance, although the element of intent has been relaxed to a degree. In fraud cases the Ohio courts have uniformly required a showing of reliance, although recklessness is treated as the equivalent of intent. Finally, in 10b-5 actions the Supreme Court has held that negligence is not actionable, has left open the question whether a showing of recklessness will meet the intent requirement, and has relaxed the requirement of reliance at least in instances of fraudulent nondisclosure.

The broad remedy provision in the blue sky statute provides that "[e]very sale or contract of sale made in violation of 1707.01 to 1707.45, inclusive, of the Revised Code, is voidable at the election of the purchaser." This provision, in conjunction with 1707.44(b), which forbids *knowing* false representations of a material and relevant fact *for the purpose of selling securities* in Ohio, requires intent of the seller to defraud, but does not require a showing of reliance by the buyer. The separate action establishing the seller's liability for written misrepresentations, in contrast, requires reliance on the part of the purchaser, and either knowledge of the falsity of a representation or lack of diligence in ascertaining its truth or falsity on the part of the seller. 1707.41.

In contrast, in common law suits the Ohio courts have uniformly required a defrauded party to show his reliance on the challenged representation. *E.g., Block* v. *Block,* 165 Ohio St. 365, 135 N.E.2d 857 (1956), 24 *Ohio Jur.* 2d § 125, and cases cited. But Ohio does not require the plaintiff in a fraud action to show that the defendant knowingly made the misrepresentation upon which plaintiff relied. It is sufficient if a false representation was "made recklessly and without any knowledge or information on the subject calculated to induce such belief." *Beamer* v. *Feick,* 113 Ohio App. 264, 177 N.E. 2d 691 (1960).

In a recent 10b-5 suit the Supreme Court qualified the requirement of reliance. In *Affiliated Ute Citizens* v. *United States,* 406 U.S. 128, 154 (1972) the Supreme Court held that where failure to disclose was involved, proof of reliance was not a prerequisite to recovery; "All that is necessary is that the facts withheld be material in the sense that a reasonable investor might have considered them important in the making of this decision."

With regard to intent, our circuit held in *SEC* v. *Coffey,* 493 F.2d 1304, 1317 (6th Cir. 1974) that "section 10b of the 1934 Act does not impose liability for innocent acts but only for acts of fraud or deceit." This position was recently reaffirmed by the Supreme Court in *Ernst & Ernst* v. *Hochfelder,* 44 U.S.L.W. 4451, 4454 (March 30, 1976), where the Court held that an action will not lie under § 10(b) and Rule 10b-5 "in the absence of any allegation of 'scienter'—intent to deceive, manipulate, or defraud." [Footnote omitted.] The Court expressly left open the question whether reckless behavior is sufficient to create liability under 10b-5. 44 U.S.L.W. 4454 n.12.

Turning to the measure of damages, we find that each of the three causes of action may permit a slightly different measure of recovery. The blue sky statute contains two applicable remedy provisions.[3] The general remedy section, 1707.43, provides for the buyer's recovery of the purchase price (plus costs) if he tenders the securities back to the seller and the sale is rescinded. In

---

3. In addition, § 1707.41 provides for the liability of the director of the seller corporation, and § 1707.42 provides for the liability of an advisor to the seller.

addition, 1707.41 permits the buyer who relied on a written misrepresentation to recover the "damages sustained" due to his reliance on the false representations.

In contrast, the Ohio Courts have held that "the difference in value between the way the property was represented to be and the way it actually was at the time of the sale" is the proper measure of damages where the sale has been induced by fraud. *Wilchins* v. *Pool*, 29 Ohio App.2d 223, 224, 280 N.E.2d 396 (1971), *citing Molnar* v. *Beriswell*, 122 Ohio St. 348, 171 N.E. 593 (1930).

Finally, with regard to damages in a 10b-5 suit in the *Affiliated Ute* case the Supreme Court stated:

> In our view, the correct measure of damages under § 28 of the Act, 15 U.S.C. § 78bb(a), is the difference between the fair value of all that the . . . seller received and the fair value of what he would have received had there been no fraudulent conduct, see *Myzel* v. *Fields*, 386 F.2d 718, 748 (CA8 1967), cert. denied, 390 U.S. 951 (1968), except for the situation where the defendant received more than the seller's actual loss. In the latter case damages are the amount of the defendant's profit. See *Janigan* v. *Taylor*, 344 F.2d 781, 786 (CA1 1965), cert. denied, 382 U.S. 879 (1965).
>
> 406 U.S. 155.

In *Janigan* the circuit court distinguished between the measure of damages for a defrauded seller and a defrauded buyer:

> . . . We turn to the remedy. With respect to damages we draw a distinction between cases where, by fraud, one is caused to buy something that one would not have bought or would not have bought at that price, and where, by fraud one is induced to convey property

> to the fraudulent party. In the former case the damages are to be reckoned solely by "the difference between the real value of the property at the date of its sale to the plaintiffs and the price paid for it, with interest from that date, and, in addition, such outlays as were legitimately attributable to the defendant's conduct, but not damages covering 'the expected fruits of an unrealized speculation.'" Sigafus v. Porter, 1900, 179 U.S. 116, 125, 21 S.Ct. 34, 37, 45 L.Ed. 113. See Estate Counseling Service, Inc. v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 10 Cir., 1962, 303 F.2d 527, 533; Securities Exchange Act of 1934, 15 U.S.C. § 78bb; 3 Loss, Securities Regulation, p. 1793 (2d ed. 1961).[5] On the other hand, if the property is not bought from, but sold to the fraudulent party, future accretions not foreseeable at the time of the transfer even on the true facts, and hence speculative, are subject to another factor, viz., that they accrued to the fraudulent party. It may, as in the case at bar, be entirely speculative whether, had plaintiffs not sold, the series of fortunate occurrences would have happened in the same way, and to their same profit. However, there can be no speculation but that the defendant actually made the profit and, once it is found that he acquired the property by fraud, that the profit was the proximate consequence of the fraud, whether foreseeable or not. It is more appropriate to give the defrauded party the benefit even of windfalls than to let the fraudulent party keep them. 344 F.2d 768. [Footnotes omitted.]

This discussion suffices to make it clear that both the Ohio common law of fraud and its blue sky statute bear a marked resemblance to 10b-5, but neither is identical with it. We conclude that the common law of fraud is

sufficiently similar to the case law developing under § 10(b) and Rule 10b-5 that federal policy will be best served by the *continued* application of the four year limitation period that we approved in *Connelly* v. *Balkwill, supra*. In *IDS Progressive* we held that we should not change the limitation period applicable to 10b-5 actions without "good cause" because to do otherwise adds "unnecessary uncertainty to the prosecution of federal claims under Section 10b-5." 533 F.2d 343. Moreover, we observed that the broad remedial purposes of the federal securities acts are "best served by a longer, not a shorter statute of limitations." 533 F.2d 344. Applying these two principles to the case before us we hold that the four year fraud statute of limitations, upon which the parties may have relied, is applicable.

Accordingly, the judgment of the district court in *McIntyre* will be affirmed, and the judgment of the district court in *Nickels* will be reversed, and both cases are remanded for further proceedings consistent with this opinion.

IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF OHIO
WESTERN DIVISION

March 27, 1975

No. C 74-309

CHARLES NICKELS, et al.,
Plaintiffs,

-vs-

KOEHLER MANAGEMENT CORPORATION, et al.,
Defendants.

OPINION AND ORDER

WALINSKI, J:

This cause is before the Court upon a motion by all defendants to dismiss the case pursuant to Rule 12(b)(6), Federal Rules of Civil Procedure, on the grounds that the suit is barred by the appropriate statute of limitations. All concerned have briefed the matter.

This is a suit under the Securities Exchange Act of 1934 [hereinafter the Exchange Act], 15 U.S.C., § 78 *et seq.* in which a right to relief is claimed under § 10(b) of the Exchange Act and Rule 10b-5 promulgated thereunder. Plaintiff claims that he and the class of shareholders he seeks to represent suffered damages as the result of material, false and misleading statements, and the failure by defendants to disclose material facts in the merger of two corporations, American Insurance Management Corporation [hereinafter AIMC] and Ohio Indiana Mutual Corporation [hereinafter OIMC], into what is now known as Koehler Management Corporation. It is claimed that defendants failed to disclose to the shareholders the facts that OIMC had loaned defendant Koehler, who was

President of both OIMC and AIMC at the time, in excess of $590,000, that there was insufficient security and reserves for the loan, that it constituted a major asset of OIMC, and that it was of doubtful collectibility and had therefore precariously weakened OIMC. Despite knowledge of these facts, it is claimed that the defendant directors approved the merger of the two corporations and recommended shareholder approval. The statement to the shareholders failed to include any of this information, and the merger was approved on May 8, 1970. Plaintiffs claim they only discovered the allegedly fraudulent acts in January, 1971.

The statute and rule on which relief is sought contain no statute of limitations. It is thus the federal policy to adopt an appropriate local law of limitations. 28 U.S.C., § 1652; *United Auto Workers* v. *Hoosier Cardinal Corp.*, 383 U.S. 696 (1966); *Cope* v. *Anderson*, 331 U.S. 461 (1947); *Holmberg* v. *Armbrecht*, 327 U.S. 392 (1946); *Campbell* v. *Haverhill*, 155 U.S. 610 (1895). In *Connelly* v. *Balkwill*, 174 F. Supp. 49, 63-4 (N.E. E.D. Ohio 1959), *aff'd*, 279 F.2d 685 (1960), the Eastern Division of this Court applied the general fraud statute of limitations, § 2305.09, Ohio Revised Code, in a suit under § 10(b) and Rule 10b-5. There was no suggestion in that case that another statute in the Ohio Blue Sky Law might apply, and the choice was merely between the general fraud statute and another one limiting actions brought on a liability created by a statute.

Then in *Charney* v. *Thomas*, 372 F.2d 97 (6th Cir. 1967), the Sixth Circuit again applied the general Michigan fraud statute of limitations. In so doing, the court said that while in some cases the local Blue Sky statute of limitations might be more appropriate, it would decline to use the Michigan statute because Michigan law contained

no provision similar to § 10(b). But the court began by noting that as of that time no other court had ever applied a Blue Sky Law limitations provision.

Since then the reverse is nearly true. Decisions in the Fifth, Seventh and Eighth Circuits have now applied Blue Sky Law statutes of limitations in preference to fraud statutes. *See Hudak* v. *Economic Research Analysts, Inc.*, 499 F.2d 996 (5th Cir. 1974); *Parrent* v. *Midwest Rug Mills, Inc.*, 455 F.2d 123 (7th Cir. 1972); and *Vanderboom* v. *Sexton*, 422 F.2d 1233 (8th Cir.), *cert. denied*, 400 U.S. 825 (1970). As articulated in *Hudak* the rule applied by these Courts, representing the modern weight of authority, appears to be:

> "[t]he limitation period which the forum state applies to the state remedy which bears the closest substantive resemblance to Rule 10b-5 and which best effectuates its purpose is to be applied." *Hudak* v. *Economic Research Analysts, Inc., supra* at 999.

Plaintiffs' argument herein runs as follows: *Connelly* v. *Balkwill, supra,* and *Charney* v. *Thomas, supra,* are still the law in this Circuit.[1] Under these holdings, this Court should apply the general fraud statute of limitations, § 2305.09, Ohio Revised Code; and that period is four years. Since, under *Holmberg* v. *Armbrecht, supra,* the running of a state statute in federal securities law cases is governed by the federal equitable doctrine which tolls the statute until the fraud is discovered, and since the fraud herein, if any, was discovered in January, 1971, this case was timely filed in August, 1974, and is not barred by § 2305.09. Plaintiffs further argue that even if *Charney* and *Connelly* could be said to have been under-

1. *See also Toledo Trust Co., etc.* v. *Nye*, Civil No. C 72-281 (N.D. W.D. Ohio, Memorandum Opinion filed Feb. 25, 1975), per Young, J., which followed the *Charney* rule.

mined by *Hudak* and other decisions, the Ohio Blue Sky Law contains no provision similar to § 10(b) and Rule 10b-5 since the Ohio provisions uniformly require proof of scienter while the federal provisions do not. Therefore, § 2305.09 is still the most appropriate statute to apply.

Defendants contend otherwise. They argue that *Charney* and *Connelly* are both outdated and, in essence, that the Sixth Circuit would follow *Hudak* were it deciding the issue today. They further contend that the Court should look to the Ohio Blue Sky Law limitations and apply the relevant statute, § 1707.43[2], Ohio Revised Code, to the facts of this case. That section contains a two-year limitations period. Since the fraud, if any, was discovered in January, 1971, this case was not timely filed in 1974 and must be dismissed.

After a careful examination of these arguments and authorities, this Court has concluded that defendants should prevail. Initially, the Court concludes that plaintiffs' reliance on *Charney* and *Connelly* is misplaced.

In *Connelly,* the plaintiffs first sued on their claim in an Ohio state court and based their claim on common law fraud. After losing in the trial court, they also lost in the Ohio appellate courts. Only then did they file their action in federal court. While alleging essentially the same facts, they based their right to relief on § 10(b) and Rule 10b-5. In claiming that the action was barred by the statute of limitations, as well as by the doctrine of res judicata, defendants did not suggest that the Court

2. "No action for the recovery of the purchase price as provided for in this section, and no other action for any recovery based upon or arising out of a sale or contract for sale made in violation of sections 1707.01 to 1707.45, inclusive, of the Revised Code, whether based on a contract or tort, and whether legal or equitable in nature, shall be brought after two years from the date of such contract of sale."

apply an Ohio Blue Sky Statute of Limitations, because the claim was arguably barred by even the more generous fraud limitations. The limitations issue turned instead on whether the limitations period of § 2305.07, Ohio Revised Code, which deals with suits on a liability created by a statute, should be applied instead of the fraud limitations. Thus, the Court had no occasion whatever to deal with the specific issue now faced by this Court. It is thus difficult for this Court to understand how plaintiffs could therefore have assumed that *Connelly* would control this issue and thus rely thereon that they would have four years to file their complaint.

In *Charney,* plaintiffs sued in federal court claiming a right to relief under § 16(b), and apparently under the Michigan common law of fraud as well. The district judge dismissed the case on the basis that the plaintiffs' sole remedy on the state claim lay under the state Blue Sky Law, and that claim was barred by the state two-year Blue Sky statute of limitations on rescission. The court also held that the federal claim was barred by the same statute, rather than the fraud limitations. The Sixth Circuit reversed the district court on both counts.

As to the latter, the Sixth Circuit appears to have been strongly influenced by the utter lack of case authority preferring the Blue Sky limitations. This is illustrated by an examination of the cases cited by the court. 372 F.2d at 100.

In *Janigan* v. *Taylor,* 344 F.2d 781 (1st Cir. 1965), the only question was whether the Massachusetts statute of limitations being applied was tolled until the fraud was discovered. The court ruled that it was under the now generally recognized doctrine of *Holmberg* v. *Armbrecht.*

In *Fratt* v. *Robinson*, 203 F.2d 627 (9th Cir. 1953), the issue was whether the applicable statute was the general fraud statute of limitations or the one limiting actions on a liability created by statute. In preferring the former, the *Janigan* court appeared to be holding that § 10(b) and Rule 10b-5 do nothing more than condemn common law fraud when it is carried out by the mails or an instrumentality of interstate commerce, a proposition now suspect.

The court in *Azalea Meats, Inc.* v. *Muscat*, 246 F. Supp. 780 (S.D. Fla. 1965), *rev'd on other grounds*, 386 F.2d 5 (5th Cir. 1967), preferred a Florida statute limiting actions on a liability created by statute to the fraud limitations; while this court in *Connelly* v. *Balkwill, supra*, had decided the same issue contra.

Given this internal inconsistency of authorities, it is clear that the Sixth Circuit was influenced by the nearly total failure of anyone even to raise the issue of Blue Sky Law applicability as well as the absence of case law. As previously shown, however, this is no longer so; and the recent circuit decisions prefer the various Blue Sky Law limitations periods. For these reasons, this Court concludes that *Charney* and *Connelly* do not mandate an application of § 2305.09 to this case; and the Court will now consider which limitations law applies.

The Court begins with the premise that any limitations period chosen must be one which best effectuates the federal policies underlying the federal securities laws. Of course, to determine those policies, the Court turns to the statutes themselves.

That the Securities Act of 1933 and the Securities Exhcange Act of 1934 are remedial acts which must be broadly construed to effect their purposes goes without

saying. And the Supreme Court has only recently confirmed that these acts were intended by Congress "to be construed not technically and restrictively, but flexibly to effectuate [their] remedial purposes." *Affiliated Ute Citizens* v. *United States*, 406 U.S. 128, 150 (1972).

Although § 10(b) of the Exchange Act contains no limitations provision, every other provision of the two Acts which creates a civil liability does contain a limitatons period.[3] *See, e.g.*, 15 U.S.C., § 77m (one year for actions for failure to register, one year from discovery or three years from sale on actions by buyers for material omissions or misstatements); 15 U.S.C., § 78ii(e) (one year from discovery and three years from event on actions based on manipulative and fraudulent actions on a national securities exchange); 15 U.S.C. § 78r (similiar one and three year provisions for actions based on false or misleading statements in filings with the SEC); and 15 U.S.C., § 78cc(b) (same with respect to actions seeking to void contracts made in violation of the Exchange Act or any rule thereunder).

This virtually unbroken pattern of limitations of one year from discovery and absolute bar after three years from sale or other event strongly suggests a Congressional policy favoring short limitations periods rather than the longer ones found in many states' common law fraud statutes. Moreover, the subject of Congressional attention in these Acts is an item of highly fluctuating value with rapid overnight changes. That Congress was aware of this is apparent in § 2(3) and (4) of the Exchange Act where Congress twice speaks of "sudden and unreasonable fluctuations" in the price of securities. Unduly long limita-

---

3. This analysis is suggested in Martin, "Statutes of Limitations in 10b-5 Actions: Which State Statute is Applicable?", 29 Bus. Law. 443 (1974).

tions periods would appear to permit those who claim to be aggrieved by violations of the Act to lie in wait for the stock market to take a propitious turn before they visit the courthouse. While this Court has little sympathy for those who prey on the gullible and the unwary, the fact that Congressional policy is to protect the innocent investor does not mean that Congress also intended to favor one who "loses his innocence and waits to see how his investment turns out before he decides to invoke [the Act]." *Royal Air Properties* v. *Smith*, 312 F.2d 210 (9th Cir. 1962); and *Hecht* v. *Harris, Upham & Co.*, 283 F. Supp. 417 (N.D. Cal. 1968).

And finally, since Congress has included registration, reporting and disclosure provisions throughout the Acts, it appears that Congress has sought to facilitate the discovery of fraud by the reasonably vigilant investor. For these reasons, the Court concludes that it is the policy of the federal laws involved herein to favor a relatively short statute of limitations in selecting among the state statutes arguably applicable and to toll the statute until discovery.

Applying the "resemblance" test used in *Hudak* v. *Economic Research Analysts, Inc., supra,* and *Parrent* v. *Midwest Rug Mills, supra,* it is at once apparent that § 1707.44 bears a closer resemblance to an action under Rule 10b-5 than it does to an action in common law fraud and deceit.[4] Plaintiffs make the sweeping assertion that the scienter requirement of a fraud action and § 1707.44 is now no longer a part of a Rule 10b-5 action. This Court is less sure of the existence of the scienter require-

4. This test cannot be considered at odds with anything in *Charney* v. *Thomas*, because there the Sixth Circuit itself declared that the feedral courts must apply the state statute "which best effectuates the federal policy at issue." 372 F.2d at 100.

ment in a Rule 10b-5 action than is plaintiff. However, it is not necessary to decide that issue in order to find a closer resemblance in § 1707.44, because the Ohio Blue Sky Law deals with the same subject, with largely the same goals and underlying policies, as do the federal securities laws. It is a specific statutory scheme dealing with the same subject as the federal scheme, while an action in fraud and deceit is not so limited. The mere fact that both the Ohio Blue Sky Law and a common law fraud action require proof of scienter, while Rule 10b-5 may not, does not serve to make the fraud statute more appropriate. Since both have the scienter requirement, this only points up more clearly the need for federal legislation. In any case, to borrow from the Fifth Circuit:

> "federal courts borrow only the chronometric aspects and not the procedural or substantive nuances of the forum." *Wolf* v. *Frank*, 477 F.2d 467, 475 (5th Cir. 1973).

The Court feels it necessary to discuss one final matter. As previously noted, Judge Young of this very Court has very recently decided this precise issue in favor of the Ohio fraud statute rather than the Blue Sky Law. *Toledo Trust Co.* v. *Nye, supra.* However, it appears in that case that Judge Young was primarily influenced by two matters.

First, in that case the plaintiff was the personal representative of a seller of securities who was deceased. In part, it was claimed that the decedent was wronged by the failure of the defendants to disclose to the decedent the fact that the company whose securities they sought to purchase had received merger proposals from another company and that proposed merger would have enhanced the value of the securities in the hands of the decedent. In reading the Ohio Blue Sky Law, Judge Young concluded

that the plaintiff therein had no remedy thereunder whatever and that his sole state remedy lay, presumably, under an action in fraud and deceit. Thus, under the resemblance test used herein, it might be argued that the fraud limitations was used because it was the only statute which resembled the remedy provided by Rule 10b-5.

Secondly, it appears that the alleged fraud in *Nye* was discovered on August 13, 1970, and the action was filed on August 18, 1972; so that the plaintiff, an executor of the defrauded decedent's estate, was only late in filing by a period of five days if one applied the two-year limitations of § 1707.43. This Court prefers to view Judge Young's decision as an application of the "flexibility" commanded by *Affiliated Ute Citizens, supra,* and the equity notions, as discussed in *Holmberg* v. *Armbrecht, supra,* which lie at the heart of a federal court's use of a state statute of limitations in an action where the rights and liabilities are created by federal law. As Mr. Justice Frankfurter said:

> "[s]uch statutes have been drawn upon by equity solely for the light they may shed in determining that which is decisive for the chancellor's intervention, namely whether the plaintiff has inexcusably slept on his rights so as to make a decree against the defendant unfair. * * * A federal court may not be bound by a State statute of limitation and yet that court may dismiss a suit where the plaintiffs' 'lack of diligence is wholly unexcused; and both the nature of the claim and the situation of the parties was such as to call for diligence * * *.'" *Id.* at 396.

Thus, the Court finds the *Nye* decision distinguishable from the case at bar, since there are no similar equitable principles operating in favor of plaintiffs here.

For the foregoing reasons, the Court holds that plaintiffs' claims herein are barred by application of the Ohio Blue Sky Law statute of limitations, § 1707.43, Ohio Revised Code, and the cause is dismissed.

IT IS SO ORDERED.

/s/ Nicholas V. Walinski
United States District Judge

Toledo, Ohio.
March 27, 1975.

FEDERAL SECURITIES LAWS

Securities Act of 1933, Section 13
15 U.S.C. § 77m

§ 77m. Limitations of Actions

No action shall be maintained to enforce any liability created under section 77k or section 77*l*(2) unless brought within one year after the discovery of the untrue statement or the omission, or after such discovery should have been made by the exercise of reasonable diligence, or, if the action is to enforce a liability created under section 77*l*(1), unless brought within one year after the violation upon which it is based. In no event shall any such action be brought to enforce a liability created under section 77k or section 77*l*(1) more than three years after the security was bona fide offered to the public, or under section 77*l*(2) more than three years after the sale.

Securities Act of 1933, Section 17(a)
15 U.S.C. § 77q(a)

§ 77q. Fraudulent Interstate Transactions

(a) It shall be unlawful for any person in the offer or sale of any securities by the use of any means or instruments of transportation or communication in interstate commerce or by the use of the mails, directly or indirectly—

(1) to employ any device, scheme, or artifice to defraud, or

(2) to obtain money or property by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(3) to engage in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon the purchaser.

Securities and Exchange Act of 1934, Section 9(e)
15 U.S.C. § 78i(e)

§ 78i. Prohibition Against Manipulation of Security Prices

* * *

(e) Any person who willfully participates in any act or transaction in violation of subsection (a), (b), or (c) of this section, shall be liable to any person who shall purchase or sell any security at a price which was affected by such act or transaction, and the person so injured may sue in law or in equity in any court of competent jurisdiction to recover the damages sustained as a result of any such act or transaction. In any such

suit the court may, in its discretion, require an undertaking for the payment of the costs of such suit, and assess reasonable costs, including reasonable attorneys' fees, against either party litigant. Every person who becomes liable to make any payment under this subsection may recover contribution as in cases of contract from any person who, if joined in the original suit, would have been liable to make the same payment. No action shall be maintained to enforce any liability created under this section, unless brought within one year after the discovery of the facts constituting the violation and within three years after such violation.

Securities and Exchange Act of 1934, Section 10(b)
15 U.S.C. § 78j(b)

§ 78j. Manipulative Deceptive Devices

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange—

* * *

(b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

Securities and Exchange Commission Rule 10b-5
17 C.F.R. 240.10b-5

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of

interstate commerce, or of the mails, or of any facility of any national securities exchange,

(1) To employ any device, scheme, or artifice to defraud,

(2) to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(3) to engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person,

in connection with the purchase of sale of any security.

Securities and Exchange Act of 1934, Section 18(c)
15 U.S.C. § 78r(c)

§ 78r. Liability for Misleading Statements

* * *

(c) No action shall be maintained to enforce any liability created under this section unless brought within one year after the discovery of the facts constituting the cause of action and within three years after such cause of action accrued.

Securities and Exchange Act of 1934, Section 27
15 U.S.C. § 78aa

§78aa. Jurisdiction of offenses and suits

The district courts of the United States, and the United States courts of any Territory or other place subject to the jurisdiction of the United States shall have exclusive jurisdiction of violations of this chapter or the rules and regulations thereunder, and of all suits in equity and actions at law brought to enforce any liability or duty created

by this chapter or the rules and regulations thereunder. Any criminal proceeding may be brought in the district wherein any act or transaction constituting the violation occurred. Any suit or action to enforce any liability or duty created by this chapter or rules and regulations thereunder, or to enjoin any violation of such chapter or rules and regulations, may be brought in any such district or in the district wherein the defendant is found or is an inhabitant or transacts business, and process in such cases may be served in any other district of which the defendant is an inhabitant or wherever the defendant may be found. Judgments and decrees so rendered shall be subject to review as provided in sections 225 and 347 of Title 28. No costs shall be assessed for or against the Commission in any proceeding under this chapter brought by or against it in the Supreme Court or such other courts.

Securities and Exchange Act of 1934, Section 29(b)
15 U.S.C. § 78cc(b)

§ 78cc. Validity of contracts

* * *

(b) Every contract made in violation of any provision of this chapter or of any rule or regulation thereunder, and every contract (including any contract for listing a security on an exchange) heretofore or hereafter made, the performance of which involves the violation of, or the continuance of any relationship or practice in violation of, any provision of this chapter or any rule or regulation thereunder, shall be void (1) as regards the rights of any person who, in violation of any such provision, rule, or regulation, shall have made or engaged in the performance of any such contract, and (2) as regards the rights of any person who, not being a party to such contract, shall have acquired any right thereunder with actual

knowledge of the facts by reason of which the making or performance of such contract was in violation of any such provision, rule, or regulation: *Provided*, (A) That no contract shall be void by reason of this subsection because of any violation of any rule or regulation prescribed pursuant to paragraph (2) or (3) of subsection (c) of section 78*o* of this title, and (B) that no contract shall be deemed to be void by reason of this subsection in any action maintained in reliance upon this subsection, by any person to or for whom any broker or dealer sells, or from or for whom any broker or dealer purchases, a security in violation of any rule or regulation prescribed pursuant to paragraph (1) of subsection (c) of section 78*o* of this title, unless such action is brought within one year after the discovery that such sale or purchase involves such violation and within three years after such violation.

OHIO REVISED CODE

Chapter 1707: Securities

§ 1707.01 Definitions.

As used in sections 1707.01 to 1707.45, inclusive, of the Revised Code:

• • •

(J) "Fraud," "fraudulent acts," "fraudulent practices," and "fraudulent transactions" mean anything recognized on or after July 22, 1929, as such in courts of law or equity; any device, scheme, or artifice to defraud or to obtain money or property by means of any false pretense, representation, or promise; any fictitious or pretended purchase or sale of securities; and any act, practice, transac-

tion, or course of business relating to the sale of securities which is fraudulent or which has operated or would operate as a fraud upon the purchaser.

§ 1707.40 Civil liabilities. (GC § 8624-43)

Sections 1707.01 to 1707.45, inclusive, of the Revised Code create no new civil liabilities, and do not limit or restrict common law liabilities for deception or fraud other than as specified in sections 1707.41, 1707.42, and 1707.43 of the Revised Code, and there shall be no civil liabilities for noncompliance with orders, requirements, rules, or regulations made by the division or securities under section 1707.19, 1707.20, and 1707.23 of the Revised Code.

§ 1707.41 Civil liability of seller for fraud. (GC § 8624-35)

In addition to the other liabilities imposed by law any person who, by a written or printed circular, prospectus, or advertisement, offers any security for sale, or receives the profits accruing from such sale, is liable, to any person who purchased such security relying on such circular, prospectus, or advertisement, for the loss or damage sustained by such relying person by reason of the falsity of any material statement contained therein, unless such offerer or person who receives the profits establishes that he had no knowledge of the publication thereof prior to the transaction complained of, or had just and reasonable grounds to believe such statement to be true. Whenever a corporation is so liable, each director of the corporation is likewise liable unless he shows that he had no knowledge of the publication complained of, or had just and reasonable grounds to believe the statement therein to be true. Any such director, upon the payment by him of a judgment so obtained against

him, shall be subrogated to the rights of the plaintiff against such corporation, and shall have the right of contribution for the payment of such judgment against such of his fellow directors as would be individually liable under this section. Lack of reasonable diligence in ascertaining the fact of such publication or the falsity of any statement contained in it shall be deemed knowledge of such publication and of the falsity of any untrue statement in it.

No action brought against any director, based upon the liability imposed by this section, shall be brought more than two years after the purchase of securities by the person so damaged or after the payment of the judgment for which contribution is sought.

§ 1707.42 Civil liability of adviser. (GC § 8624-36)

Whoever, with intent to secure financial gain to himself, advises and procures any person to purchase any security, and receives any commission or reward for such advice or services without disclosing to the purchaser the fact of his agency or his interest in such sales, shall be liable to such purchaser for the amount of such purchaser's damage thereby, upon tender of such security to, and suit brought against, such adviser, by such purchaser. No such suit shall be brought more than one year subsequent to such purchase.

§ 1707.43 Remedies of purchaser in unlawful sale. (GC § 8624-48a)

Every sale or contract for sale made in violation of sections 1707.01 to 1707.45, inclusive, of the Revised Code, is voidable at the election of the purchaser. The person making such sale or contract for sale, and every person

who has participated in or aided the seller in any way in making such sale or contract for sale, are jointly and severally liable to such purchaser, in an action at law in any court of competent jurisdiction, upon tender to the seller in person or in open court of the securities sold or of the contract made, for the full amount paid by such purchaser and for all taxable court costs, unless the court determines that the violation did not materially affect the protection contemplated by the violated provision.

No action for the recovery of the purchase price as provided for in this section, and no other action for any recovery based upon or arising out of a sale or contract for sale made in violation of sections 1707.01 to 1707.45, inclusive, of the Revised Code, whether based upon contract or tort, and whether legal or equitable in nature, shall be brought after two years from the date of such sale or contract for sale.

No purchaser is entitled to the benefit of this section who has failed to accept, within thirty days from the date of such offer, an offer in writing made after two weeks from the date of such sale or contract of sale, by the seller or by any person who has participated in or aided the seller in any way in making such sale or contract of sale, to take back the security in question and to refund the full amount paid by such purchaser.

§ 1707.44 Violations.

(A) No person shall engage in the business of acting as broker for others in the purchase or sale of securities, sell securities, cause them to be sold, offer them for sale, cause them to be offered for sale, or engage in the business of buying, selling, or dealing in securities otherwise than

in transactions through or with a licensed dealer, unless the securities are of a kind specified in division (G) or (I) of section 1707.02 of the Revised Code, the transactions are of a kind specified in divisions (B) to (L), inclusive, and (O) to (Q), inclusive, of section 1707.03 of the Revised Code, or in section 1707.04 or 1707.06 of the Revised Code, or the transactions are exempt under section 1707.34 of the Revised Code, without being licensed by the division of securities.

(B) No person shall knowingly make or cause to be made any false representation concerning a material and relevant fact, in any oral statement or in any prospectus, circular, description, application, or witten statement, for any of the following purposes:

(1) Complying with sections 1707.01 to 1707.45, inclusive, of the Revised Code, in regard to registering securities by description;

(2) Securing the qualification of any securities under such sections;

(3) Procuring the licensing of any dealer or salesman under such sections;

(4) Selling any securities in this state

(C) No person shall knowingly and intentionally sell, cause to be sold, offer for sale, or cause to be offered for sale, any security which comes under any of the following descriptions:

(1) Is not exempt under section 1707.02 of the Revised Code, nor the subject matter of one of the transactions exempted in sections 1707.03, 1707.04, and 1707.34 of the Revised Code, has not been registered by description or qualified, and is not the subject matter of a transaction that has been registered by description;

(2) The prescribed fees for registering by description or for qualification have not been paid in respect to such security;

(3) Such person has been notified by the division, or has knowledge of such notice, that the right to buy, sell, or deal in such security has been suspended or revoked, or that the registration by description or by qualification under which it may be sold has been suspended or revoked;

(4) The offer or sale is accompanied by a statement that the security offered or sold has been or is to be in any manner indorsed by the division.

(D) No person who is an officer, director, or trustee of, or a dealer for, any issuer, and who knows such issuer to be insolvent in that the liabilities of such issuer exceed its assets, shall sell any securities of or for any such issuer, without disclosing the fact of such insolvency to the purchaser.

(E) No person with intent to aid in the sale of any securities on behalf of the issuer, shall knowingly make any representation not authorized by such issuer or at material variance with statements and documents filed with the division by such issuer.

(F) No person, with intent to deceive, shall sell, cause to be sold, offer for sale, or cause to be offered for sale, any securities of an insolvent issuer, with knowledge that such issuer is insolvent in that the liabilities of such issuer exceeds its assets, taken at their fair market value.

(G) No person in selling securities shall knowingly engage in any act or practice which is, in sections 1707.01 to 1707.45, inclusive of the Revised Code, declared illegal, defined as fraudulent, or prohibited.

Chapter 2305: Jurisdiction; Limitation of Actions

§ 2305.09 Four years; certain torts. (GC § 11224)

An action for any of the following causes shall be brought within four years after the cause thereof accrued:

(A) For trespassing upon real property;

(B) For the recovery of personal property, or for taking or detaining it;

(C) For relief on the ground of fraud;

(D) For an injury to the rights of the plaintiff not arising on contract nor enumerated in sections 2305.10 to 2305.12, inclusive, 2305.14, and 1307.08 of the Revised Code.

If the action is for trespassing under ground or injury to mines, or for the wrongful taking of personal property, the causes thereof shall not accrue until the wrongdoer is discovered; nor, if it is for fraud, until the fraud is discovered.

FILED
JAN 3 1977
MICHAEL RODAK, JR., CLERK

Supreme Court of the United States

October Term, 1976

No. 76-751

KOEHLER MANAGEMENT CORP., GERALD KOEHLER, ROGER BENHAM, WILLIAM J. EISENHAUER, PAUL M. GILLMOR, MARTIN A. JANIS, ROBERT B. JOHNSTON, RAY W. MOLDER, ALFRED E. RHODEN, M. D., GILBERT H. SIEGEL, RAY L. VISCHER, Estate of JOSEPH A. SCHUSTER, Deceased,

Petitioners,

vs.

CHARLES NICKELS and MARGARET NICKELS on Behalf of Themselves and All Other Shareholders of Koehler Management Corporation,

Respondents.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

BRIEF FOR RESPONDENTS IN OPPOSITION

DENNIS E. MURRAY
JAMES L. KIMBLER
MURRAY & MURRAY CO., L.P.A.
300 Central Avenue
Sandusky, Ohio 44870
Telephone: 1-419-627-9700
Attorneys for Respondents

THE GATES LEGAL PUBLISHING CO., CLEVELAND, OHIO—TEL. (216) 621-5647

TABLE OF CONTENTS

Reasons for Denying the Writ 1

I. There Is No Conflict Between the Decision of the Sixth Circuit in Nickels and the Decisions of Other Circuits 1

II. The Petitioners Have Not Set Forth Any Good Reasons to Overturn the Established Law on This Issue in the Sixth Circuit 6

III. Adoption of Statutes of Limitations Found in Other Sections of the Federal Securities Act Would Create Uncertainty in the Law 9

Conclusion 10

TABLE OF AUTHORITIES

Cases

Affiliated Ute Citizens v. United States, 406 U.S. 128 (1972) 8

Charney v. Thomas, 372 F.2d 97 (6th Cir. 1967) 2, 3, 4, 6, 7, 9

Clegg v. Conk, 507 F.2d 1351 (10th Cir. 1974), *cert. denied*, 422 U.S. 1007, 95 S. Ct. 2628, 45 L.Ed.2d 669 (1975) 9

Connelly v. Balkwell, 279 F.2d 685 (6th Cir. 1960) 6, 7

Douglas v. Glenn E. Hinton Investment, Inc., 440 F.2d 912 (1971) 9-10

Ernest and Ernest v. Hochfelder, ... U.S. ....., 47 L.Ed.2d 668, 96 S. Ct. ..... (1976) 7-8

Hudak v. Economic Research Analysts, Inc., 499 F.2d 996 (5th Cir. 1974), *cert. denied*, 419 U.S. 1122, 95 S. Ct. 805, 42 L.Ed.2d 821 (1975) 2, 4, 5, 6, 8, 9

IDS Progressive Fund, Inc. v. First of Michigan Corporation, 533 F.2d 340 (6th Cir. 1976) 7, 9
Janigan v. Taylor, 344 F.2d 781 (1st Cir. 1965) 9
John Hopkins University v. Hutton, 488 F.2d 912 (4th Cir. 1973) 9
Klein v. Shields & Co., 470 F.2d 1344 (2nd Cir. 1972) .. 9
Kubik v. Goldfield, 479 F.2d 472 (3rd Cir. 1973) 9
Parrent v. Midwest Rug Mills, Inc., 455 F.2d 123 (7th Cir. 1972) 2, 3, 4, 5, 6, 9
S. E. C. v. Coffey, 493 F.2d 1304 (6th Cir. 1974) 5
Trussell v. United Underwriters Ltd., 228 F. Supp. 757 (1964) 3
United California Bank v. Salik, 481 F.2d 1012 (9th Cir. 1973), *cert. denied*, 414 U.S. 1004 (1973) 7, 8, 9
Vanderboom v. Sexton, 422 F.2d 1233 (8th Cir. 1970) 2, 4, 6, 9

Statutes

Ark. Stat. Ann. Sections 67-1235 through 1262 2
Ark. Stat. Ann. Section 67-1256 (Replacement 1966) 2
Mich. Stat. Ann. Sec. 19.760; Comp. Laws 1948, Section 451.120 3
Ohio Revised Code, Section 2305.09 ..... 6, 7
Ohio Revised Code, Section 1707.43 8
Ohio Revised Code, Section 1707.01, et seq. 8
Securities Act of 1933, 15 U.S.C. Section 77(l) (2) 2
Securities Act of 1933, 15 U.S.C. Section 12(2) 2
Uniform Securities Act, Section 410 2

Supreme Court of the United States

October Term, 1976

No. .....

KOEHLER MANAGEMENT CORP., GERALD KOEHLER, ROGER BENHAM, WILLIAM J. EISENHAUER, PAUL M. GILLMOR, MARTIN A. JANIS, ROBERT B. JOHNSTON, RAY W. MOLDER, ALFRED E. RHODEN, M. D., GILBERT H. SIEGEL, RAY L. VISCHER, Estate of JOSEPH A. SCHUSTER, Deceased,

Petitioners,

vs.

CHARLES NICKELS and MARGARET NICKELS on Behalf of Themselves and All Other Shareholders of Koehler Management Corporation,

Respondents.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

BRIEF FOR RESPONDENTS IN OPPOSITION

REASONS FOR DENYING THE WRIT

I. There Is No Conflict Between the Decision of the Sixth Circuit in Nickels and the Decisions of Other Circuits.

The first reason given by the petitioners in the petition regarding why this Court should hear this case is that the decision of the Sixth Circuit below is in conflict with

the decisions of other circuits. A reading of the decisions cited by the petitioners shows that there are significant differences between those cases and the present case. An understanding of those differences is essential to understanding why there is, in reality, no conflict between the decision of the Sixth Circuit in this case and the decisions cited by the petitioners. The cases involving 10b-5 actions cited by the petitioners are, from the Fifth Circuit, *Hudak v. Economic Research Analysts, Inc.*, 499 F.2d 996 (1974); from the Seventh Circuit, *Parrent v. Midwest Rug Mills, Inc.*, 455 F.2d 123 (1972); and, from the Eighth Circuit, *Vanderboom v. Sexton*, 422 F.2d 1233 (1970).

Of these, the first one to apply a statute of limitations found in a state blue sky statute was *Vanderboom v. Sexton*, 422 F.2d 1233 (Eighth Circuit—1970). That case arose in Arkansas and involved a choice between the Arkansas statute of limitations for blue sky actions and a general statute of limitations which has been made applicable to fraud. In that case, the Federal District Court for the Western Division of Arkansas had applied the statute of limitations found in Arkansas' blue sky law (Ark. Stat. Ann. Sections 67-1235 through 1262). The particular section of Arkansas' blue sky law involved in the case was Ark. Stat. Ann. Sec. 67-1256 (Replacement 1966). This statute is Section 410 of the Uniform Securities Act. Section 410 is modeled after and parallels Section 12(2) of the Securities Act of 1933, 15 U.S.C. Section 77(1) (2). The limitation period in this section is two years; and, as a result, the plaintiffs' claim was barred. On appeal the plaintiffs argued that the proper statute of limitations to apply was that statute applicable to action for fraud because Rule 10b-5 and Section 67-1256 of the Arkansas blue sky statute were not identical. The appellant cited to *Charney v. Thomas*, 372 F.2d 97 (Sixth Circuit—1967), in which the Sixth Circuit in a Michigan case

had held that the proper statute in 10b-5 actions was the Michigan statute of limitations applicable to actions for fraud and not the statute of limitations found in Michigan's blue sky laws (Mich. Stat. Ann. Sec. 19.760; Comp. Laws 1948, Sec. 451.120). The appellants also cited to a case from the Federal District Court in Colorado: *Trussell v. United Underwriters Ltd.*, 228 F. Supp. 757 (1964), in which the Court had rejected the application of a state blue sky statute of limitations and had applied the state statute of limitations governing actions for fraud. The Eighth Circuit, however, applied the Arkansas blue sky statute and distinguished the cases cited by the appellant by reasoning that the basis for the decisions in *Charney* and *Trussell* was that those courts construed Rule 10b-5 as requiring scienter and, thus, basically analogous to common law fraud. The Court pointed out that the rule in the Eighth Circuit was that Rule 10b-5 applied to negligent, as well as intentional, misrepresentations and then held that the statute of limitations found in Arkansas' blue sky law should be applied. Consequently, the Eighth Circuit stated that this called for a shorter limitation period on the federal claim (422 F.2d 1239). A close reading of the opinion shows that this was the most important factor in its decision, although the Court did mention other factors, such as a commonalty of purpose between Rule 10b-5 and the Arkansas blue sky statute and the same lack of defense under Rule 10b-5 and the Arkansas statute.

The next Circuit Court of Appeals to hold that a state blue sky statute of limitation should be applied in a Rule 10b-5 case was the Seventh Circuit in *Parrent v. Midwest Rug Mills, Inc.*, 455 F.2d 123 (1972). In that case, which arose in Illinois, the Seventh Circuit applied the statute of limitations found in the Illinois blue sky law. In its opinion, the Seventh Circuit cited to *Charney*

and *Vanderboom* as holding that in 10b-5 actions the statute of limitations for the statute most closely resembling Rule 10b-5 should be applied (455 F.2d 126). The Seventh Circuit then stated that the divergent results of the two cases could be explained by the differing interpretation of Rule 10b-5 in the Sixth and Eighth Circuits. The Seventh Circuit looked upon *Charney* as holding that in Rule 10b-5 actions the plaintiff must prove scienter while the Eighth Circuit in *Vanderboom* read Rule 10b-5 in a broader sense, holding that negligent, as well as intentional, conduct was actionable under Rule 10b-5. The Seventh Circuit then stated that it agreed with the Eighth Circuit's interpretation of Rule 10b-5 and held that the statute of limitations contained in the Illinois blue sky statute should be applied (455 F.2d 126). Although the Seventh Circuit did not express it clearly in its opinion, it is obvious from a reading of the opinion that it did agree with the Eighth Circuit that Rule 10b-5 covers negligent, as well as intentional, acts.

The final Circuit Court of Appeals opinion involving Rule 10b-5 cited by the petitioners is the opinion of the Fifth Circuit in *Hudak v. Economic Research Analysts, Inc.*, 499 F.2d 996 (1974). In *Hudak*, a Florida case, the Fifth Circuit chose to apply a blue sky statute of limitations. In so doing, the Court stated that: "We concur in the reasoned judgment of the Seventh and Eighth Circuits which, when faced with the present choice . . . found the similarity between the blue sky and 10b-5 scienter requirements crucial to their decisions." (499 F.2d 1000). As in *Vanderboom* and *Parrent*, the opinion in *Hudak* reflects the relationship between the decision to lower the standard of culpability required for a 10b-5 violation and the decision to choose the shorter state statute of limitations. This relationship exists because implicit in the opinions of the Fifth, Seventh, and Eighth

Circuit Courts of Appeals is the belief that statutes of limitations governing lawsuits based upon non-culpable conduct should be shorter than those governing lawsuits based upon culpable conduct. Historically this has been true in American jurisprudence. The reason that longer statutes of limitations govern intentional wrongdoing is to be certain that such tortfeasors are forced to compensate their victims. Short statutes of limitations would work against the exposure of these wrongdoers to suit.

Unlike the Seventh and Eighth Circuits, the Sixth Circuit had never held a purely negligent tortfeasor to be accountable under Rule 10b-5. In *S. E. C. v. Coffey*, 493 F.2d 1304 (1974), the Sixth Circuit stated that non-culpable conduct would not constitute Rule 10b-5 violation ". . . since Section 106 of the 1934 Act does not impose liability for negligent acts but only for acts of fraud and deceit." (493 F.2d 1304). Since the Sixth Circuit had always regarded Rule 10b-5 violations as fraudulent acts requiring scienter, the policy considerations which had led the other circuits to impose a relatively short statute of limitations were not present in this case. Besides the difference between the Fifth, Seventh, and Eighth Circuits and the Sixth Circuit on the issue of the necessity of scienter in Rule 10b-5 violations, another difference exists between this case and the opinions in *Parrent* and *Hudak*. The language of the blue sky statutes involved in those two cases was virtually identical to the language of Section 10 (B) and Rule 10b-5. A reading of those opinions shows that those Courts were influenced by that fact. *Parrent v. Midwest Rug Mills, Inc.*, 455 F.2d 123, 127; and *Hudak v. Economic Research Analysts, Inc.*, 499 F.2d 996, 1000. The Ohio blue sky statutes, while perhaps similar to Section 10 (B) and Rule 10b-5, are not so similar as to be said to parallel Section 10 (B) and Rule 10b-5.

Understanding the rationale of the decisions of the Fifth, Sixth, Seventh, and Eighth Circuits, it at once becomes apparent that the "conflict" which petitioners allege exists is a result of the different interpretations put upon Rule 10b-5 by those circuits. The opinions of the Seventh and Eighth Circuits in *Parrent* and *Vanderboom* make it clear that had these circuits regarded Rule 10b-5 as covering only intentional or fraudulent acts then they would have chosen the state statute of limitations for actions based on fraud. The opinion of the Fifth Circuit in *Hudak* shows that that circuit also regarded its determination that Rule 10b-5 encompasses a lesser standard of culpability than does fraud as being crucial to its decision to choose the Florida statute covering blue sky violations.

II. The Petitioners Have Not Set Forth Any Good Reasons to Overturn the Established Law on This Issue in the Sixth Circuit.

In 1960 the Sixth Circuit affirmed in *Connelly v. Balkwell*, 279 F.2d 685, an opinion of the Federal District Court for the Northern District of Ohio. The Federal District Court had held that the state statute of limitations to be applied in a private action based on Rule 10b-5 was the statute of limitations found in Section 2305.09 of the Ohio Revised Code. That case did not involve a choice between that statute of limitations and the one found in the Ohio securities law. Seven years thereafter, however, the Sixth Circuit again had the opportunity to consider the statute of limitations issue. *Charney v. Thomas*, 372 F.2d 97 (1967), did involve a choice between applying the six-year Michigan limitations for fraud and a two-year limitation found in the state blue sky law. In *Charney*, the Sixth Circuit held that the Michigan blue sky

statute did not contain a provision similar to Rule 10b-5 and, therefore, that the statute of limitations to be applied was the one governing fraud actions. As a result of these two cases, parties in Ohio had reason to believe that the proper statute of limitations to be applied in a Rule 10b-5 case was the one found in Ohio Revised Code Section 2305.09. Although it is true that *Connelly* did not involve the same issues as the present case, nevertheless, the two cases, when taken together, constitute the law governing Rule 10b-5 cases in Ohio.

Most recently, in *IDS Progressive Fund, Inc. v. First of Michigan Corporation*, 533 F.2d 340 (Sixth Circuit—1976), the Sixth Circuit held that "[f]or us to change the applicable limitations period without good cause would add an unnecessary uncertainty to the prosecution of federal claims under Section 10 (B)." (533 F.2d 343). Consequently, the Court refused to apply the new Michigan blue sky limitations contained in the Uniform Securities Act, which limitations had been adopted in place of the earlier blue sky law considered in *Charney*. The Court also held that: "The broad remedial purposes of the federal securities laws are best served by a longer, not a shorter, statute of limitations." [533 F.2d 344, quoting *United California Bank v. Salik*, 481 F.2d 1012 (Ninth Circuit—1973), *cert. denied*, 414 U.S. 1004 (1973)]. Obviously, the same policy reasons for not adopting the state statute of limitations urged by the petitioners are present in this case. What "good cause" exists in this case to justify overturning the *precedent* in the Sixth Circuit?

The petitioners argue that the decision below is in conflict with the decision of other circuits and should be reversed by this Court. That "conflict", however, as shown above, does not, in reality, exist. Indeed, since the decision of this Court in *Ernest and Ernest v. Hoch-*

felder,..... U.S....., 47 L.Ed.2d 668, 96 S. Ct. ..... (1976), the underlying rationale of the decisions cited by the petitioners no longer exists. Also, as noted earlier, the present case is unlike *Hudak*, which involved a statute that is virtually identical to Section 10 (B) and Rule 10b-5.

What is really important, however, is not what the statute looks like but which statute best effectuates the federal policy behind Rule 10b-5. The petitioners argue that the statute of limitations found in Ohio Revised Code Section 1707.43 best effectuates the federal policy of Section 10 (B) and Rule 10b-5. In the section of their petition covering that issue, however, they never really state how the statute of limitations found in Section 1707.43 best effectuates federal policy. Most of that section alleges that Section 1707.01, et seq., most resembles Section 10 (B) and Rule 10b-5. As the Sixth Circuit observed in the case below, however, in Ohio an action based on common law fraud is very similar to an action based on Rule 10b-5. The Sixth Circuit noted that both the Ohio blue sky statute and Ohio actions for common law fraud ". . . bear a marked resemblance to 10b-5, but neither is identical with it." (page A15 of the Appendix Opinion of *Nickels v. Koehler Management Corporation*). As this Court noted in *Affiliated Ute Citizens v. United States*, 406 U.S. 128 (1972), the federal securities act serves a "broad remedial purpose". This purpose is complemented by private actions for Rule 10b-5 violations. By choosing the fraud statute of limitations, the Sixth Circuit encourages the filing of Rule 10b-5 actions and increases the deterrent aspects of private litigation under Rule 10b-5. This conclusion was also reached by the Ninth Circuit in *United California Bank*.

III. Adoption of Statutes of Limitations Found in Other Sections of the Federal Securities Act Would Create Uncertainty in the Law.

The last reason given by the petitioners for this Court to hear this case is that the federal policy underlying the implied remedy of Section 10 (B) and Rule 10b-5 would be best effectuated by applying the statute of limitations found in other parts of the Federal Securities Act. The argument in this section of the petition is that the use of statutes of limitations contained in other parts of the Federal Securities Act would prevent "unfairness" to plaintiffs (allegedly resulting from differences between the various circuits) and would be more in keeping with the intent of Congress. As the Sixth Circuit noted in *IDS Progressive*, every Circuit Court of Appeals that has considered the issue has applied a state statute of limitations in a Rule 10b-5 action. See *Janigan v. Taylor*, 344 F.2d 781 (First Circuit—1965); *Klein v. Shields & Co.*, 470 F.2d 1344 (Second Circuit—1972); *Kubik v. Goldfield*, 479 F.2d 472 (Third Circuit—1973); *John Hopkins University v. Hutton*, 488 F.2d 912 (Fourth Circuit—1973); *Hudak v. Economic Research Analysts, Inc.*, 499 F.2d 996 (Fifth Circuit—1974), *cert. denied*, 419 U.S. 1122, 95 S. Ct. 805, 42 L.Ed.2d 821 (1975); *Charney v. Thomas*, 372 F.2d 97 (Sixth Circuit—1967); *Parrent v. Midwest Rug Mills, Inc.*, 455 F.2d 123 (Seventh Circuit—1972); *Vanderboom v. Sexton*, 422 F.2d 1233 (Eighth Circuit—1970); *United California Bank v. Salik*, 481 F.2d 1012 (Ninth Circuit), *cert. denied*, 414 U.S. 1004, 94 S. Ct. 361, 38 L.Ed.2d 240 (1973); *Clegg v. Conk*, 507 F.2d 1351 (Tenth Circuit—1974), *cert. denied*, 422 U.S. 1007, 95 S. Ct. 2628, 45 L.Ed.2d 669 (1975). For this Court to now hold that state statutes of limitations should not be applied would cause great uncertainty to litigants and their counsel. As the Ninth Circuit wrote in *Douglas v. Glenn E. Hinton Investment*,

Inc., 440 F.2d 912 (1971): "Reasonable stability in laws pertaining to voluntary relationships between parties, and the right of access to the courts to question those relationships, is a worthwhile objective." (440 F.2d 916).

There may be a theoretical appeal to commentators in choosing statutes of limitations found in other parts of the Federal Securities Act; but, in the everyday world of commerce, stability in the law, as noted by the Ninth Circuit, is very necessary. If this Court were to make such a change, it would only lead to greater confusion in this area. The agent for such a change, if such a change is desirable, is Congress. It would have the advantage of being able to secure a great many opinions and to express its true intent in this area. Just as importantly, the public would be aware of the effect of such a change and would be able to plan accordingly. Finally, action by Congress to change the limitation period would avoid litigation as to the effective date of such change and as to the effect of such change on pending actions.

CONCLUSION

For the foregoing reasons, it is respectfully submitted that this petition for a writ of certiorari should be denied.

DENNIS E. MURRAY
JAMES L. KIMBLER
MURRAY & MURRAY CO., L.P.A.
300 Central Avenue
Sandusky, Ohio 44870
Telephone: 1-419-627-9700
Attorneys for Respondents